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PRESENTATION

Operator

Good morning, and welcome to the Simmons First National Corporation Third Quarter Earnings Conference Call. (Operator Instructions) Please note, this event is being recorded. I would now like to turn the conference over to Ed Bilek, Executive Vice President and Director of Investor Relations. Please go ahead.

Edward J. Bilek - *Simmons First National Corporation - Executive VP & Director of IR*

Good morning, and welcome to Simmons First National Corporation's Third Quarter 2022 Earnings Call. Joining me today are several members of our executive management team, led by our Chairman and CEO, George Makris. Before we begin the Q&A, I would like to remind you that our third quarter earnings materials, including the release and presentation deck, are available on our website at simmonsbank.com under the Investor Relations tab.

During today's call, we will make forward-looking statements about our future plans, goals, expectations, estimates, projections and outlook including, among others, our outlook regarding future economic conditions, interest rates, lending and deposit activity and net interest margin. These statements involve risks and uncertainties, and you should, therefore, not place undue reliance on any forward-looking statements as actual results might differ materially from those expressed in or implied by the forward-looking statements due to a variety of factors.

Additional information concerning some of these factors is contained in our earnings release and investor presentation furnished with our Form 8-K today, our most recent Form 10-Qs and our Form 10-K for the year ended December 31, 2021, including the risk factors contained in that form 10-K. These forward-looking statements speak only as of October 25, 2022, and Simmons assumes no obligation to update or revise any forward-looking statements or other information.

Finally, in this presentation, we will discuss certain non-GAAP financial metrics we believe provide useful information to investors. Additional disclosures regarding non-GAAP metrics, including the reconciliations of these non-GAAP metrics to GAAP are contained in our earnings release and investor presentation, which are included as exhibits to the Form 8-K we filed this morning with the SEC and are also available on the Investor Relations page of our website, simmonsbank.com. Operator, we are ready to begin the Q&A session.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question is from Brady Gailey of KBW.

Brady Matthew Gailey - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

So loan growth was pretty impressive in the third quarter in the low double-digit range. I know you guys have talked about that moderating from here. But how do you think about loan growth as we head into 2023 with some potential economic uncertainty?

Matthew Steven Reddin - *Simmons First National Corporation - Executive VP & Chief Banking Officer of Simmons Bank*

Brady, this is Matt. I'll point you back to our second quarter comments and really that what we said, we started to see the fallout from the rising interest rates kind of the end of the second quarter where we delivered some really impressive loan growth. Throughout the third quarter, 2 Fed hikes, 150 basis points, and it's really illustrating our pipeline on Page 12, where that pipeline is now $1.6 billion, that's really a result of the staying disciplined to our relationship strategy, underwriting hurdles, stress tests.

And it's still a strong pipeline, but it's definitely reflective of current economic conditions, but we've had a lot of success in the construction space. So I think we'll continue to see some loan growth in the fourth quarter and on, but just depending on what the Fed does, I think I just look back at what happened between the second and third quarter and what the increase in interest rates did to our pipeline.

And if you have another 150 basis points, I think that's something we look at as we move forward. But loan growth is going to continue through some construction but moderate as interests continue to move up.

Brady Matthew Gailey - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Okay. All right. And then on the expense side, if you look at kind of core expenses when you back out the one-timers, it was pretty flat. It's actually down a little bit linked quarter at $137 million. How are you thinking about expense creep into 2023?

James M. Brogdon - *Simmons First National Corporation - Executive VP, CFO & Treasurer*

Well, I think -- Brady, this is Jay. I'll jump in on that with some initial remarks. I think we'll continue to fight the good fight that everyone is fighting on the inflation front. Again, we've had some tailwinds as it relates to acquisitions over the last handful of quarters, and we continue to identify opportunities and execute on sort of extracting the efficiencies from those transactions.

But look, the inflationary environment is real I think we'll have to stay focused there. I'm pleased to see our efficiency ratio moving in a good direction. I think we'll continue to see that throughout '23. But I think we'll see the same battle that everyone else is seeing, especially on the wage inflation front. So far, I'm pretty pleased with how we've been able to combat that.

I think we've still got some opportunities to combat that. So I don't think it's runway expenses, but we'll stay disciplined there and stay focused on it.

Brady Matthew Gailey - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

All right. And then finally for me, the share buyback did not slow at all in the third quarter. It was still at pretty robust level, repurchasing about 1.5% of the company. How do you -- your TCE now has a 6th handle on it. So how do you think about the buyback going forward?

Robert A. Fehlman - *Simmons First National Corporation - President & COO*

Well, Brady, this is Bob. I would tell you, we continue to have the buyback as part of our capital management plan. As always, we'll evaluate each quarter as we go in. So I think it will be part of our plan in the future, but we'll evaluate where we are going forward. We look at TCE, we look also at all our regulatory capitals, which are well above well capitalized and so in good shape there.

So it's just overall management. What we will say is our plan. We won't buy back any more than our current earnings in the quarter, paying back both cash dividends and stock buyback. Again, not saying that's what we'd do this quarter, but it is part of our management strategy.

Operator

The next question is from David Feaster of Raymond James.

David Pipkin Feaster - *Raymond James & Associates, Inc., Research Division - VP & Research Analyst*

Maybe just starting on deposits. I'm just curious how you think about deposit flows near term, what you're seeing there? And your strategy as you think about managing deposits, obviously, we're much better positioned in this cycle with a lower loan-to-deposit ratio. But curious how you and your Chief Deposit Officer are thinking about defending deposit costs, continuing to lock in some funding. And maybe just from a geographic perspective, if you could touch on some of the competitive dynamics and where you're seeing the most competition and funding pressure.

James M. Brogdon - *Simmons First National Corporation - Executive VP, CFO & Treasurer*

Well, David, I'll jump in on that, Jay, again here. So first of all, I'd say you hit it spot on. The competitive dynamic is evolving, has evolved meaningfully throughout the year this year. I think the competition is -- we'll continue to do that. I'll tell you, in our business, we certainly do our best, and I think we're pretty good at managing our deposits by geography that competitive landscape is different really throughout our footprint.

And so we continue to keep a pretty tailored approach to how we run that area of the business. But overall, what I'd tell you is for our experience in Q3 and really throughout kind of this tightening cycle thus far, where we see deposits leaving the bank, it's really customers who have excess cash. So that may be commercial customers with operating accounts and historically haven't had a place, at least in recent history to put that money to work or high net worth customers, those types of customers have options today.

We're doing our best and having some success in keeping some of those -- some of that revenue in-house by deploying our wealth group in some of those situations and moving those deposits off balance sheet and into the wealth group. But that's really where we see -- it's not really customer attrition.

It's just sort of excess funds that are leaving. And so we'll we will be as aggressive as we can be within reason. We're here to kind of fight and protect margin. Good news is asset prices or repricing have repriced significantly this year. So we've got some room from a margin perspective to keep some of those funds on the balance sheet. But that's really the experience I feel like we've had thus far.

David Pipkin Feaster - *Raymond James & Associates, Inc., Research Division - VP & Research Analyst*

Okay. And then maybe just touching on asset quality. You've done a great job managing credit. We've seen continued improvement in credit metrics. Maybe just as you look into your portfolio and maybe the economy more broadly, is there anything that you're seeing that's causing you any concern or that you're watching more closely?

And I guess, how do you think that plays into reserves and provision? I mean do you think that the reserve ratio has probably dropped here just given the likelihood for worsening inputs in CECL models?

George A. Makris - *Simmons First National Corporation - Chairman & CEO*

David, this is George. I'll touch on that and the other guys can jump in if they want to. So if you recall, we said last quarter that we had 5 specific categories where we had qualitative adjustment factors that we had carried since COVID began. Those were hotels, retail, restaurants, student housing, office space.

And during this quarter, we took a look at individual loans, and we eliminated 3 of those categories for additional category-specific adjustments. What we did keep in place were retail and office space because those 2 are going to have a tail on them, that we just don't understand quite yet with renewals of leases and whatnot. You probably noticed that we significantly increased our reserve for unfunded commitments, partially because that number went up. But also, that's where construction resides.

And we believe between retail, office space and construction, while we have a good feeling about that, those are the 3 areas that we just have some additional uncertainty in the future about.

So our Moody's scenario was skewed toward the downside S2 scenario. But our quantitative model spit out a number less than 1%. So we feel very good about where our allowance is today. We believe, as some of that construction funds going forward, you may see a migration from our reserve for unfunded commitments to our actual allowance for credit losses.

But collectively, we've got $240 million of allowance set aside for our funded and unfunded loan balances. Our credit guys do a fantastic job of stress testing and evaluating our credit. And you can see that over time, those numbers continue to go down. And I will remind you that even those numbers are heavily dependent on credit we acquired from other banks and not necessarily credit that was initially approved under Simmons underwriting standards. So I guess what I'm saying is uncertainty is certainly something that is prevalent in the market today. But based on our analysis, we're very comfortable with where we are today.

David Pipkin Feaster - *Raymond James & Associates, Inc., Research Division - VP & Research Analyst*

That makes sense. And then maybe switching gears to touch on fee income. Look, this has been an emphasis for you all in the past. It's great to see the hard work showing up. Maybe if you could just touch on some of the fee income businesses, where you're having the most success. And obviously, we do have some headwinds in the market for a few of these. Just curious how you think about fee revenues and any other trends in other puts and takes within the fee income lines would be helpful.

James M. Brogdon - *Simmons First National Corporation - Executive VP, CFO & Treasurer*

Yes. I'll give a couple of remarks there as well, David. I think, look, no doubt it was a good quarter of fee income for us. And certainly don't want to discount that at all. I will say in the wealth management area, we're having some really good success there, both on the hiring front as well as just sort of in the customer acquisition front.

There were, however, in the quarter -- there was a couple of fee events in the quarter in the wealth area that were a little bit timing related. And so probably a quarter -- and this is going to happen from time to time, but a quarter that was maybe a little bit ahead of our typical run rate, that's an area that is certainly a headwind area. I think we're cutting through some of that headwind again on kind of the customer acquisition and the sales side of that business.

So feel good about that in the quarter there. It was good to see moderate, albeit, but an uptick on a linked-quarter basis in mortgage. That's just a tough business right now, but it's one we're committed to. It's very in-footprint customer-centric focus to us. Virtually all of that business in this environment is overwhelming majority of its purchase volume.

So we feel good about what we have there. And then they'll just be the typical seasonality that will impact kind of service charges and deposit-related fees from time to time. We had a good quarter there. I think one of the tailwinds for us late in Q3, hopefully, it will stick a little bit in Q4 as well as just some of the waivers and whatnot that we did around the Spirit acquisition that are phasing off here late in Q3 and in Q4. So that certainly aided us on the fee front late in the quarter as well.

Operator

Next question is from Gary Tenner of D.A. Davidson.

Gary Peter Tenner - *D.A. Davidson & Co., Research Division - MD & Senior Research Analyst*

I wanted to follow up on the commentary, George, around the construction portfolio, $5.1 billion of unfunded commitments this quarter, you mentioned a large amount of that is in the construction book. Can you talk about kind of how much is commercial versus residential? And I'm really curious about any commentary around projects that are being maybe delayed or terminated as the economic uncertainty increases and rate rise.

Matthew Steven Reddin - *Simmons First National Corporation - Executive VP & Chief Banking Officer of Simmons Bank*

This is Matt. I can start on that, and 1 can jump in. A couple of comments. When you think about the $5 billion unfunded commitments, that's all of our unfunded. That's our lines of credit. That's our C&I businesses. When you really look into the construction book itself, it's about $3 billion unfunded. And of that $500 million is your 1 to 4. That's your builder finance area. And if you think about kind of your question on kind of where is it coming from a lot of that business that we -- as far as the last 6 months of originations has been in industrial and multifamily.

And both of those segments are holding up very, very well in this environment with affordability pushing into multifamily and supply chain industrial. So like where we've put our capital in the construction. And then on your question around delays, we're not seeing that, and we have a pretty robust monitoring system outside of our daily bankers, kind of a centralized function.

And we look at that very carefully. And so far, outside of this, what I want to now call it, normal supply chain issues, no significant delays where we're now concerned. Projects are on scheduled release. So, so far, so good. And I'll just also point you to our comments we've made in Q2, we're very disciplined in this space. I mean we are not betting on interest rates, mean we're underwriting at well above where rates are today and then stressing those further plus inflationary costs. And so when those size out, you're really producing a low, low leveraged construction loan that's on our books.

Gary Peter Tenner - *D.A. Davidson & Co., Research Division - MD & Senior Research Analyst*

I appreciate the comment. And then second question, in terms of the rate sensitivity, Slide 16. I'm curious, as you think of the next 100 basis points of tightening since you provide 100 basis points to 200 basis point sensitivity, what deposit betas are embedded in that kind of next 100 basis points that [aim] your sensitivity?

James M. Brogdon - *Simmons First National Corporation - Executive VP, CFO & Treasurer*

Yes. And I'll answer that consistent with how I have historically, the way we model this, right, wrong or indifferent is based on historical betas. So it's not really a forward-looking beta. It's not a management override. And so when we look at that historical beta for us and for the industry, you're seeing betas in kind of the mid-40s that are modeled into this sensitivity, but much higher than what our beta has been year-to-date.

Gary Peter Tenner - *D.A. Davidson & Co., Research Division - MD & Senior Research Analyst*

And that's total deposit beta, correct? Not interest bearing.

James M. Brogdon - *Simmons First National Corporation - Executive VP, CFO & Treasurer*

Man. Yes, that's right. I do believe that's a total deposit beta. That's right. Yes.

Operator

The next question is from Matt Olney of Stephens.

Matthew Covington Olney - *Stephens Inc., Research Division - MD & Analyst*

I want to go back to the loan growth discussion. And Matt, you gave us some good commentary about construction balance is likely to fund up in the near term. Is it fair to assume that loan growth could remain in this low double-digit range annualized as far as the growth in the fourth quarter and then likely slow into '23, just given the overall uncertainty in the economy?

Matthew Steven Reddin - *Simmons First National Corporation - Executive VP & Chief Banking Officer of Simmons Bank*

Matt, I think that's a reasonable assumption. I can't say that for certain, for sure. Just knowing, I'll repeat my comment again, we saw 150 basis points upward rate increases in the third quarter and seeing that may be expected to happen again. I mean, yes, with our unfunded construction, yes, that's out there. But we're also seeing borrowers pay down in this environment. So there's a little things that we can't really anticipate, but that's a reasonable expectation. And just depending on where the Fed moves after that, I point you back to our pipeline graph and show you where we're taking our yields and where the pipeline is moving in this environment.

James M. Brogdon - *Simmons First National Corporation - Executive VP, CFO & Treasurer*

Yes. And I'll just pile on to that, Matt, this is Jay here. Maybe just one additional comment. We're, of course, I'm sure every other management team out there is doing the same thing. We're spending a lot of time forecasting, doing a lot of sensitivity analysis here. And I think the first thing we've got to acknowledge is these are these are pretty uncertain macro times in terms of creating conviction around those forecasts and that predictability.

And just listening to Matt Reddin's comments there, I think one of the big levels of unpredictability is just money flows, cash flows here, timing of some of these fund ups. We're not modeling many prepayments right now, but we see some from time to time. And so we know what our scheduled maturities and cash flows look like. But when you think about sort of deposit flows, deposit repricing some of these loans and loan originations and fund-ups. Timing of cash flows are pretty interesting to look at right now. And that's not going to be for us. I think that's just -- I think that will be industry-wide.

Matthew Covington Olney - *Stephens Inc., Research Division - MD & Analyst*

Yes. Understood. And then I guess on the betas on the loan balances, they looked pretty good in the third quarter. Anything unusual with that from your perspective? Or you think you can maintain similar-ish kind of loan betas going forward from here?

Matthew Steven Reddin - *Simmons First National Corporation - Executive VP & Chief Banking Officer of Simmons Bank*

I would say I'll take first and let Jay comment. Matt, we are being very disciplined with our pricing models still in the relationship business and we have an avenue to always make sure we take care of core customers, but we're very fitted to the market. I mean we're adjusting our rates on it sometimes every 2 weeks, and we remain disciplined in the field with communication to our bankers and ultimately our clients. So I think we're going to fight that fight. And we're hopeful that we'll go to continue to do that on the yield side, on field side.

James M. Brogdon - *Simmons First National Corporation - Executive VP, CFO & Treasurer*

Yes. And one thing I'd just point out to, when you think about our loan beta or even just sort of net interest margin, and we depict this on Slide 6 in the materials. But our revenue growth, our margin, net interest income this quarter is really through the headwind of kind of a $5.5 million unfavorable variance compared to Q2 from a purchase accounting accretion or PPP accretion point of view.

So I think some of those underlying fundamentals are even a little bit masked in Q3 compared to Q2. And then just one other data point, Matt, that I'd give you. It's also in our slides. It's all the way back on -- oh goodness, is it 17? 16.

Yes. On '16, we've got a comment that I want to point everybody to. And that's just the fact that I mentioned earlier, timing of cash flows, scheduled maturities. We've got $1.2 billion of fixed rate loans that will mature over the next 12 months. All in, I think we've probably got at least probably $1.8 billion in fixed rate assets that will mature or come up for reprice or reinvest over the next 12 months.

And so when I think about where we're pricing assets today and where those yields are be coming off the books, I think that continued sort of migration or optimization of our balance sheet and repricing on the asset side will be pretty good for us.

Matthew Covington Olney - *Stephens Inc., Research Division - MD & Analyst*

And Jay, following up on that, just lots of puts and takes around the margin from the third quarter. And I'm thinking about the core margin ex, some of the noise you talked about. It feels like there's still some tailwinds here over the next few quarters of the margins to see some improvement. Any commentary on any kind of range you point us towards?

James M. Brogdon - *Simmons First National Corporation - Executive VP, CFO & Treasurer*

Well, I'm going to go back to my initial caveat, which is timing and cash flows, could drive that, I think, on a quarter-to-quarter basis of exactly what margin itself might do. But in general, I think the industry has gapped up pretty nicely in Q2 and Q3 from a margin perspective, and we've experienced that as well. My expectation is that margin will be much more modest or incremental in terms of its expansion going forward.

I certainly think that's our expectation over the course of the next several quarters. But it's -- I think that we've all had the good fortune of a really steep move by the Fed with a nice lag in deposit betas, and that's just going to moderate itself for the industry, I believe, over the coming quarters. And so I think the NIM expansion will be more modest as well.

Operator

The next question is from Graham Dick of Piper Sandler.

Graham Conrad Dick - *Piper Sandler & Co., Research Division - Research Analyst*

Most of my questions have been answered, but I just wanted to touch on the bond portfolio a little bit. Obviously, a big step down this quarter, I guess, on help fund from that robust loan growth. Just wondering if you guys have got -- I don't know an update on the target, maybe you guys see this trending too on assets over the next, I don't know, year or so?

James M. Brogdon - *Simmons First National Corporation - Executive VP, CFO & Treasurer*

Well, I think we're certainly not active purchasing bonds just given where we are from a securities mix point of view or securities to assets point of view and really given the opportunities we have in the loan portfolio right now. Our first priority from an investment point of view with our funds is always to put that to work in the loan portfolio if we have good opportunities we underwrite through the cycle, as Matt was talking about earlier. So we're not really having to change our underwriting standards.

They just are what they are, and we're still experiencing good growth and really good pricing. And so that's where our priority will be. And with that, kind of with all of those statements, we'll continue to see, I think, the loan-to-deposit ratio increase. loan-to-asset numbers will expand and we'll fund a lot of that growth with cash flows out of that securities portfolio.

Graham Conrad Dick - *Piper Sandler & Co., Research Division - Research Analyst*

Okay. Understood. And then on loan growth, I guess, I just wanted to -- if I remember correctly, Spirit was growing pretty well after you guys announced a deal and then close on. I'm just wondering how much of that pipeline is from Spirit, the commercial loan pipeline?

Matthew Steven Reddin - *Simmons First National Corporation - Executive VP & Chief Banking Officer of Simmons Bank*

Great question. I'll kind of give you a couple of data points as you think about their growth. As a company of our loan growth, they did -- they've grown $230 million since they've been a part of Simmons in April. So that's not -- that's more than the third quarter. They've also done $1 billion of new production. So we're real proud of how Spirit came into our organization and hit the ground running. And if you look at their overall pipeline right now, they're around $400 million of our $500 million fully in of our overall pipeline.

James M. Brogdon - *Simmons First National Corporation - Executive VP, CFO & Treasurer*

And maybe just to pile on, on the deposit side, one of the things we paid real close attention to is overall deposit retention, which has been incredibly strong. So I think you see it both on the -- candidly, on the employee retention front, which is where it matters most, has been great. Deposit retention has been really strong. And then Matt's comments on the loan and loan origination side. So yes, we're very pleased there across the board.

Operator

There are no other questions at this time. This concludes our question-and-answer session. I would like to turn the conference back over to George Makris for closing remarks.

George A. Makris - *Simmons First National Corporation - Chairman & CEO*

Well, thanks to each of you for joining us today. I think the third quarter speaks very well to our organic fundamentals and what we're committed to going forward. I think our runway looks really, really good. Before we sign off, I'd like to give a special shout out to one of our directors, Dean Bass, who was involved in a pretty serious car accident a few weeks ago and is recovering in the hospital. Today, I've visited with him this morning, he's in great spirits. And we just want to give a shout out to Dean, wish him all the best in his speedy recovery. So thanks, again, for joining us this morning, and we'll do this again next quarter.

Edward J. Bilek - *Simmons First National Corporation - Executive VP & Director of IR*

Before we end today's call, I have been advised by our legal counsel that there were some technical difficulties during our forward-looking statement. So we would like to reiterate that during the call today, we did make forward-looking statements about our future plans, goals, expectations, estimates, projections and outlooks among others, our outlook regarding future economic conditions, interest rates, lending and deposit activity and net interest margin.

These statements involve risks and uncertainties and you should therefore, not place undue reliance on any forward-looking statements as actual results could differ materially from those expressed in or implied by the forward-looking statements due to a variety of factors. Those factors are contained in our 8-K that was filed today as well as our other SEC filings, including our Form 10-Q and Form 10-K.

These forward-looking statements are as of October 25, 2022, and Simmons assumes no obligation to update or revise any forward-looking statements or other information. We also did discuss certain GAAP and non-GAAP metrics, and we have provided disclosure in our Form 8-K in our earnings release and in our investor deck that contains the reconcilements of those metrics from GAAP to non-GAAP. Thank you again for joining us, and have a good day.

Operator

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