NASDAQ – WSFS

Moderator: Beth Sellers
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1:00 p.m. ET

Operator: This is conference # 59503237.

Operator: Good day, ladies and gentlemen, and welcome to the WSFS Financial Corporation's third quarter 2015 earnings call.

At this time all participants are in a listen only mode. Later we will conduct a question-and-answer session and instructions will follow at that time. If anyone should require assistance during the call, please press star then zero on your touchtone telephone to reach an operator.

As a reminder, today's conference is being recorded. I would now like to introduce your host for today, Mr. Rodger Levenson, Chief Financial Officer. Sir, you may begin.

Rodger Levenson: Thank you, (Liz). Thanks to all of you for taking time to participate in our call today.

With me on this call are Mark Turner, President and CEO; Paul Geraghty, Chief Wealth Officer; Steve Clark, Chief Commercial Banking Officer, and Rick Wright, Chief Retail Banking Officer.

Before Mark begins with his opening remarks, I would like to read our Safe Harbor Statement. Our discussion today will include information about our management's view of future expectations, plans, and prospects that constitute forward-looking statements.

Actual results may differ materially from historical results or those indicated by these forward-looking statements. Due to risks and uncertainties, including, but not limited to, the risk factors included in our annual report on Form 10-K and our most recent quarterly reports on Form 10-Q. As well as other documents we periodically file with the Securities and Exchange Commission.

With that read, I'll turn it over to Mark Turner, our President and CEO.

Mark Turner: Thanks, Rodger. Thanks everyone on the call for your time and attention.

We are pleased to have reported Net Income of $14.4 million, and earnings per Share of $0.51 for the third quarter of 2015. Return on the Assets was a very healthy 1.14 percent, and Return on Tangible Common Equity was a strong 13.3 percent.

Excluding the non-core items of securities gains and corporate development expenses, Earnings were an even stronger $0.53 per Share in the quarter. And in our routine quarterly analysis, provided in our investor deck, after normalizing for the non-core items mentioned and increasing our expenses for a more normal amount of credit costs, we internally peg our core sustainable ROA at 1.16 percent for the third quarter of 2015.

All significant areas of the bank showed strength this quarter, in the year-over-year comparisons.

Net interest income increased 12 percent over the same quarter last year, (and 5 percent non-annualized over the second quarter of 2015), on growth and an improved mix of loans, investments and deposits; net interest income was also enhanced by improved performance from purchased loans and reverse mortgages. (We've noted yields on these assets can be uneven from quarter to quarter.)

The margin for the quarter was a solid 3.79 percent; that is 8 and 9 basis points better than the last quarter and this quarter last year, on the strength of that improved balance sheet mix, and those enhanced yields.

Credit quality continued its long-term positive trend. Charge-offs were elevated, primarily as a result of charging off the reserve on the one large commercial loan we both discussed and provided for last quarter. Otherwise, non-performing assets, non-performing loans, criticized loans and classified loans all improved, and delinquencies, (including non-performing delinquencies), were relatively flat at a low 53 basis points of loans.

Because of our mix of businesses, fee income can be more seasonal than at peer banks, so the year-over-year comparisons for fee income, and therefore total revenue, are more meaningful.

Fee income was up 7 percent this quarter year-over-year, primary on the significant improvement in fiduciary income which was up 24 percent.

As a result of the 12 percent increase in net interest income and the 7 percent increase in fee income, when combined, total core revenue was up 10 percent this quarter over the same quarter last year. As importantly, core expenses were up only 4 percent, resulting in 6 percentage points of positive operating leverage, as many of our investments over the past cycle are maturing, and we have achieved broader economies of scale. As a result, our reported efficiency ratio improved to just over 61 percent, and just under 60 percent excluding the non-core items mentioned earlier. Combining the healthy revenue growth and efficiency improvements, our core, pre-tax, pre-provision net revenue improved $4.3 million or 21 percent in this quarter from the same quarter last year. That's an over $17 million improvement on an annualized basis.

Deposits were up a healthy 2 percent in the quarter, non-annualized, on an increase of municipal and school district deposits, which typically come in this time of year, and gradually flow out over the course of the next 12 months. Loan growth in the third quarter was modest at only 2 percent annualized, and was muted by a very strong second quarter of growth, a highly competitive pricing environment, construction loans naturally moving to the permanent market, and reduced balances in mortgages held-for-sale from good mortgage banking activity.

Our business pipeline in loans continues to be strong, and we still expect mid to high single-digit loan growth for the full year 2015. Our margin, even without the enhancement this quarter that we mentioned, is showing good resilience because of a continued improvement in balance sheet mix. In addition, our fee income businesses continue to show nice pipelines and to gain strength.

On other growth fronts, we closed the acquisition of nearby Alliance Bank in Southeastern Pennsylvania in early October, which, excluding one-time costs, we expect will be immediately accretive. We closed and converted seamlessly all in the same weekend, and we are tightly on track for our expectations of: customer and balance retention, one-time cost, synergies, accretion and returns from this bolt-on opportunity.

These positives, combined with the strong positive operating leverage we have shown recently, auger well for WSFS coming very close to, if not slightly exceeding our three-year strategic plan goal of achieving a core sustainable 1.20 percent ROA next quarter.

We do expect next quarter will be noisy, as many one-time costs related to the October acquisition of Alliance Bank will be recognized. As usual, we will call out these and other non-core items, whether positive or negative, for your evaluation of our performance.

During the third quarter, we also continued our string of being named in an independent survey of thousands of local employees a highly-ranked “Top Workplace” in our primary market. This is the 10th year in a row we have been ranked among the top 5 workplaces in Delaware. And in a separate independent survey, we also achieved a five-year, unbroken string of being named the “number one bank” in the State from the customer's perspective. These recognitions are leading indicators of our success, and combined with our growing financial returns, which are lagging indicators of success, all of these are evidence that our strategy of Engaged Associates Delivering Stellar Service, Growing Customer Advocates and Value for our Owners is being executed well and is working well.

Finally, as a result of our strong capital earnings and prospects, we're also pleased to have announced that this quarter we completed our 5 percent share repurchase plan initiated just last October, and the Board, at its meeting yesterday, approved a new 5 percent share repurchase plan, and a 20 percent increase in our cash dividend.

Thank you for your attention. At this time, we would be happy to take your questions.

Operator: Ladies and gentlemen, if you'd like to ask a question at this time please press the star then the number one key on your touchtone telephone. If your question has been answered or you wish to remove yourself from the queue, you may do so by pressing the pound key.

Again, if you'd like to ask a question at this time, please press the star then the number one key.

Our first question comes from the line of Frank Schiraldi with Sandler O'Neill. Your line is now open, please go ahead.

Frank Schiraldi: Hi, guys. I wanted to ask about the NIM expansion linked quarter. It seems like the -- that it was a fairly stable NIM, and then and you had a couple or more one off that increased the NIM sequentially. So we should we see those increases as one offs, and that are likely to come back out of the NIM next quarter?

Rodger Levenson: Frank, it is Rodger. Yes, I think that is an accurate characterization. Those things will happen from time to time with those purchased portfolios and reverse mortgages, but they are certainly not sustainable or predictable. And as we think about our core margin for the fourth quarter, we anticipate it remaining relatively flat at around 3.70 percent.

Frank Schiraldi: OK. Just thinking about the reverse mortgage portfolio, is there any thing such as a normalized yield map portfolio, or is it just so evolved and depending on cash flows there?

Mark Turner: Yes. So if you looked at our data probably over the last three or four quarters prior to this one, our yield was fairly steady at about 17 percent on a portfolio that is declining. So this is a portfolio of purchased loans that is slowly running off over time.

It does depend on cash flows, and on the net present value calculation to determine the yield for the quarter. I would say that there is some -- as that portfolio has matured, there is some stability in it. And in fact most, and we hope most of the volatility would be to the upside for a couple reasons on the yield.

One is, we tend to be conservative in our assumptions of what will happen in that portfolio, and it is assumptions driving that present value calculation. The big assumptions there are when there will be maturity events, and that is when somebody either dies or moves out of the home. Those things are relatively predictable, but we still try and be conservative about those using actuarial tables.

The second is, what is the value of the collateral of the home when there is a maturity event and you have to sell it and recoup your loan balance, and any equity share you might have in the upside.

Fortunately for us, the most of the collateral in the portfolio that we purchased are in good places. Northern California around San Francisco, San Jose, Silicon Valley, and Southern California around San Diego and Los Angeles. And those markets have been very strong, and have outperformed our model assumptions about price appreciation. Hopefully that is helpful color.

Frank Schiraldi: Thank you. Finally, just in terms of the loan growth, I know you reiterated your guide. So that guidance is for full year 2015, if I am not mistaken?

As you look out at the pipeline and think about growth going forward, is that a fair assessment of normalized growth at this point? Maybe adjusted for any seasonality just that mid to high single-digit annual growth?

Steve Clark: Yes, Frank. This is Steve Clark. We would agree with that.

We have a very strong pipeline, 90-day weighted average of about $148 million. We feel fairly comfortable of that mid to high single-digit growth for the full year.

There are some headwinds, a couple of large construction loans will go to the permanent market in the fourth quarter also. As you know, competition is significant. But we are comfortable.

Frank Schiraldi: Great. OK, thank you.

Mark Turner: Thank you, Frank.

Operator: Our next question comes from the line of Catherine Mealor with KBW. Your line is now open.

Catherine Mealor: Thanks. Good afternoon, everyone.

Mark Turner: Good afternoon, Catherine.

Catherine Mealor: Mark, in your 1.2 percent ROA goal, how should we think about what is an appropriate assumption for total credit costs?

Mark Turner: Yes. So Rodger is more schooled on this, so I will have Rodger answer it if you don't mind.

Rodger Levenson: Yes. So in the 1.20 percent modeling that we have done, what we have been using as a normalized credit cost is going back and looking at the previous 11 quarter average, and then normalizing either up to that. Like this quarter, where we are little bit below it or down to it like we were last quarter when we had the elevated provision because of the one loan. And that number is just a little bit over $2.2 million, which is right in the middle of our long-term guidance of credit costs of between $2 million and $2.5 million for the year.

Mark Turner: Per quarter for the year.

Catherine Mealor: Got it. That is helpful. In terms of fees, any color you can give on your outlook for mortgage?

Rick Wright: Yes. Next quarter we are looking at somewhere in the $1.4 million to 41.5 million range. We were down a little bit this quarter due to slightly slower seasonal volumes, and we had some delays in delivering loans in July that backed us up a bit. But our pipeline is strong, we have got about $67 million in the pipeline so we think the $1.4 million to $1.5 million next quarter is a good number.

Catherine Mealor: OK, thank you. And then one follow-on on expenses. Can you help us frame the ALB cost savings? And if you already had the conversion, how quickly you're going to get those cost savings in the run rate next quarter?

Rodger Levenson: Yes. So when we announced the deal, we said that we expect to achieve 40 percent cost savings, 35 percent, in the first full year of the transaction. So we would expect to start seeing those impact us in the fourth quarter.

Mark Turner: And the only thing I'd add to that, it was a pretty quick clean conversion. So most of the 35 percent of the total 40 percent costs saved should come in almost right away. We do have some retention of some staff through the end of the year to take care of, obviously, issues that we'll need people to hang around a little bit for. But most of those cost savings should hit us in the fourth quarter.

Catherine Mealor: And maybe be on a full run rate by first quarter or still?

Mark Turner: I would say, for all practical purposes, we're on a full run rate by first quarter. There might be a percent or two of that 40 percent still left, but most of it will be in there.

Catherine Mealor: OK. Great. Thank you very much.

Mark Turner: Thank you.

Operator: Our next question comes from the line of Matt Schultheis with Boenning. Your line is now open.

Matt Schultheis: Good afternoon.

Mark Turner: Good afternoon, Matt.

Matt Schultheis: I was wondering if you can give us a very brief state of the state as far as how you feel the general economic conditions are doing in your markets relative to the nation as a whole? Loan demand, building, whatever you think is pertinent.

Mark Turner: So I will start at a macro level, and then I will ask Rodger and Steve and others to jump on a more macro level from a customer demand perspective. So the Delaware economy into Southeastern Pennsylvania markets we operate in continue to do fairly well. They pretty much match the national averages and trend lines on many important metrics like employment and housing activity and housing price growth. So I would characterize the local economy as not robust, but stable and slowly gathering strength.

On a big headline issue, in the state over the last month or so, there's some uncertainty about whether Chemours a DuPont spinoff, we will need to lay off some folks, and they relocate out of the state causing some job loss. And obviously, we are aware of the ongoing drama at DuPont, and the pressures that they might feel to make cost cuts resulting in layoffs and make other strategic changes.

So those are looming concerns that have not hit the markets yet. On the positive front, I think offsetting those completely if not more than completely, JPMorgan Chase just announced that over the next few years they will be adding 1,800 jobs to the state. And again, not the lower wage jobs like in the call center, but mid and higher level jobs, technology jobs, analyst, data jobs and they announced on average $65,000 a year average salary.

We continue to see those positives happening in the state, especially in the financial sector which the state is known for. Those are macro points. And I will throw it over to Steve or Rodger to talk about within our customer base what they are seeing.

Steve Clark: I would suggest, Matt, that our customer base, it's OK. I was looking back this quarter and past quarters about 70 percent of our commercial lending growth has come from existing clients, and about 30 percent has come from new relationships. And the bulk of that is really market share increases for us.

So generally, I agree with what Mark said. The economy is OK, and our customers seem to be doing OK. But certainly not robust.

Matt Schultheis: OK. That was actually the only question I had. Thank you.

Matt Schultheis: All right. Thank you.

Operator: As a reminder, ladies and gentlemen, if you'd like to ask a question at this time, please press the star then the number one key.

Our next question comes from the line of Joe Gladue with Merion Capital Group. Your line is now open.

Joe Gladue: Good afternoon.

Mark Turner: Good afternoon.

Joe Gladue: Let me take it back on the last question a little bit, just somewhat macro economically. In regards to the interest rate environment and the continued uncertainty as to whether the Fed will raise, and at least the extended period of low interest rates. Is any of that causing you to change your positioning at all, or how are you approaching that?

Mark Turner: So I will answer, and then I think Rodger can provide some details. So at this point, we entered the year being asset sensitive, with the exception of the first 100 basis 75 basis points of rate rise, because we have a WSFS prime one about $700 million of our loans that was above Wall Street Journal prime. Which we did not expect would increase as the Fed might raise rates.

As the year has progressed, we have gotten even more asset sensitive. So at this point, even over the first 75 basis points, we're not negatively affected. And to the point we're up 100 basis points, we'd see our margin increasing 3 percent, up 200 basis points 7 percent, and up 300 basis points about 10 percent.

Rodger Levenson: Actually it is at 200 percent.

Mark Turner: Excuse me.

Rodger Levenson: The first hundred is flat for us.

Mark Turner: Thank you. So after the first 100 is flat, we go up pretty significantly from there. And we've only gotten more asset sensitive as the year has gone on, as we have been adding variable-rate loans, and adding core deposits.

One of the things we have taken a look at in conjunction with the Alliance acquisition is, they bought a significant amount of liquidity to us. A lower loan-to-deposit ratio, and a lot of cash. And we used some of that cash to pay off some duration and Federal Home Loan bank advances in October, which will cost us a little bit up front on prepayment penalties, merger related, repositioning the whole balance sheet for the acquisition type costs.

But going forward, should add a couple basis points in margin and a couple of basis points in ROA just from that slight repositioning of about $100 million. And taking duration off our books and Federal Home Loan bank advances. But overall, I would say we are very well positioned for a rise in rates, and certainly would look forward to that.

The other thing I would say is this obviously all based on model data, based on betas and assumptions that we've experience in the past. We would hope to do better than the model in a rising rate environment, because the data is 10 years old. The last time rates went up, and we were a much different institution back then.

We have a much better position in the marketplace, bigger position, better branded, and we think we are a price leader in the market, now, as opposed to 10 years ago when we were more of a typical community bank and a price follower.

Joe Gladue: OK. Thank you. That is helpful.

I just have one other numbers question. On the expense side, there was a fairly significant reduction in the other non-interest expenses category. Just was wondering what that was, and if that reduction is something that was more one-time or continuing?

Rodger Levenson: Yes, Joe, it is Rodger. It is not one particular thing.

There are several areas where we had some expense reimbursements, we had Cash Connect go through its insurance deductible in the second quarter. So insurance started kicking and for them a little bit in the third quarter on theft and losses. But not any one big thing that is driving that number.

Joe Gladue: OK. But again, is some of that a more recurring reduction or again more one-time items?

Rodger Levenson: Yes, so the way I would answer that, Joe, is I would continue to think about it in the terms of our efficiency ratio, and we're in the low 60 percents. It's where we expect to stay. And as we talked about in the past, we think that's appropriate for our business model. So I think you should expect us to continue to be in that low 60 percents range.

Joe Gladue: All right. Fair enough. Thank you. That is it for me.

Mark Turner: Thank you.

Operator: Thank you. And with no further questions in queue, I'd like to turn the conference back over to Mr. Mark Turner.

Mark Turner: All right. Thanks, everybody, again. We very much appreciate your time and attention.

We are pleased to have reported the results we reported, and look forward to speaking with you this time next quarter. Rodger and I will be on the road over the next couple of weeks appearing at a couple of investor conferences and we look forward to catching up with many of you there. Have a great weekend.

Operator: Ladies and gentlemen, thank you for your participation in today's conference. This concludes the program and you may now disconnect. Everyone, have a great day.

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