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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, and welcome to the Regions Financial Corporation's quarterly earnings call. My name is Paula, and I'll be your operator for today's call. I would like to remind everyone that all participants phone lines have been placed on listen only. At the end of the call there will be a question-and-answer session. [Operator instructions]

I will now turn the call over to Mr. List Underwood to begin.

M. List Underwood
Director of Investor Relations

Thank you, operator. And good morning, everyone. We appreciate your participation in our call today. Our presenters are Grayson Hall, our Chief Executive Officer; and David Turner, our Chief Financial Officer. Other members of management are present as well and available to answer questions as appropriate. Also, as part of our earnings call, we will be referencing a slide presentation that is available under the Investor Relations section of regions.com.

Also, let me remind you that in the call and potentially in the Q&A that follows, we may make forward-looking statements which reflect our current views with respect to future events and financial performance. For further details, please reference our forward-looking disclaimer that is located in the appendix section of the presentation. With that said, I'll turn it over now to Grayson.

O. B. Grayson Hall, Jr.

Chairman, President & Chief Executive Officer

Good morning and thank you, List. I want to say just a few words about List Underwood before we get started with our financial results. As we announced earlier this week, List will be retiring at the end of the month. He's been with Regions for 23 years and has been a trusted adviser and valued member of our management team. His impressive career spans 43 years and today marks his 90 earnings call with our company. List, congratulations. We'll certainly miss you as you start your new phase in life and wish you the very best in retirement.

M. List Underwood

Director of Investor Relations

Thank you, Grayson.

O. B. Grayson Hall, Jr.

Chairman, President & Chief Executive Officer

Moving on to results. Overall, we're pleased and encouraged by our achievements and results in 2015. During the year we focused on the fundamentals, growing and deepening our customer relationships while also strengthening our financial performance by investing in initiatives that will drive revenue growth and create a more efficient and effective organization in the future. As a result, we're a much stronger organization today and are committed to continuing to build sustainable franchise value. For the fourth quarter we reported earnings from continued operations of $272 million, bringing our full year 2015 total to $1 billion. Earnings per share for the quarter totaled $0.21 per diluted share and $0.76 per diluted share for the full year. These results reflect growth and total adjusted revenue despite a challenging operating environment.

Importantly, we continue to deliver results in categories that we believe are fundamental to future income growth including checking accounts, households, Regions360 relationships and credit card accounts. For example, checking accounts grew by more than 2% during the year and active credit cards increased 11%. We remain focused on expanding and deepening relationships through our need-based approach to relationship banking and our 2015 results demonstrate that this approach is working. During the year we delivered strong average deposit growth of $3 billion, or 4%. The mix of our deposits continues to strengthen as 92% are now low-cost deposits and as we have noted before, our markets provide us with unique and competitive advantages from a deposit composition perspective.

In 2015 we achieved solid adjusted loan growth of $5 billion or 6% from the prior year. Adjusted loans and leases include a lease reclassification adjustment, which David will speak to shortly. Both business and consumer grew loans with total production for the year of $66 billion or an increase of 12% from 2014. Business lending had an excellent year growing adjusted loans 7%. Commercial banking, corporate banking and real estate banking all grew loans. And 95% of our markets achieved loan growth reflecting strength of our business models as local bankers collaborate with industry and product specialists to grow loans.

In particular, within corporate banking our specialized industries group experienced solid growth led by technology and defense as well as franchise restaurants and the real estate investment trust lending business was strong throughout the year. Consumer lending was also strong in 2015. Total loans exceeded $30 billion at year-end, an increase of 5% over 2014. Mortgage led this growth with loans increasing $496 million or 4%. Additionally, our new point of sale initiative bolstered growth in indirect lending with increased loans of $339 million. Additionally, credit card balances increased 7% from the previous year, which drove growth in card and ATM income of $30 million or 9%. Total adjusted revenue for the year increased 2% over 2014 reflecting growth in the balance sheet and investments we made to grow and diversify our revenue. Capital markets income was exceptionally strong increasing $31 million. Our recent acquisition of BlackArch Partners as well as our planned initiatives are expected to further augment capital markets income in the future.

Wealth management had a strong year with income increasing 10% over the prior year. Our focus to grow wealth management by continuing to retain, recruit and develop talent was evident in the success of our financial consultants and insurance initiatives. During 2015 we executed on our capital plan returning 93% of earnings to shareholders, which is expected to be one of the highest percentages among our peers. We also made several small but yet important investments and acquisitions in 2015 that will help drive future income. These transactions were a prudent and optimal use for our capital enabling us to expand our capabilities and product offerings to supplement future revenue growth.

With respect to the economic environment while the U.S. economy is still slow and steadily improving, there's a clear significant pressure from the global economy. Low oil prices continue to create challenges for certain industries while benefiting others. Consequently, we continue to closely monitor our energy portfolio. As expected, there continues to be downward migration in risk ratings in this portfolio. These shifts will continue if oil prices remain at current levels. However, we remain in close contact with our energy customers and believe that we're taking appropriate actions to mitigate vulnerabilities. We continue to prudently build reserves, which now stand at 6% of our direct energy exposure. As a result, we are cautious but we expect any future losses related to this portfolio to be manageable.

As we begin 2016 we remain committed to our three primary strategic initiatives. First, grow and diversify our revenue streams; secondarily, to practice disciplined expense management; and lastly, to effectively deploy our capital. These are all integral to the successful execution of our strategic plan. We continue to operate in a challenging environment that requires us to focus on what we can control. To that end, as we discussed in our Investor Day in November of last year, it's essential that we take more aggressive steps as it relates to expense management. Our goal is to eliminate $300 million of core expenses over the next three years, approximately 9% of the 2015 adjusted expense base. This plan which is underway will help us fund our initiatives and build sustainable franchise value.

In summary, 2015 was a solid year for Regions. We accomplished a great deal while laying the foundation for future earnings growth.

With that, I'll turn it over to David who will cover the details for the fourth quarter. David?

David J. Turner, Jr.

Chief Financial Officer & Senior Executive Vice President

Thank you and good morning, everyone. I'll take you through the fourth quarter details and then provide our expectations for 2016. As Grayson noted, 2015 was a solid year for Regions and the year ended particularly strong, which sets us up well for 2016. Before I get started, during the fourth quarter, Regions corrected the accounting for certain leases, which had previously been included in loans. These leases had been classified as capital leases but were subsequently determined to be operating leases. The cumulative effect on pre-tax income lowered net interest income and other financing income $15 million and reduced the net interest margin by five basis points in the quarter. The adjustment resulted in a reclassification of these leases out of loans into other earnings assets totaling approximately $834 million at the end of the quarter. The company does not expect this adjustment to have a material impact to net interest income or other financing income or net interest margin in any future reporting period.

With respect to the balance sheet, adjusted loan and lease balances totaled $82 billion at the end of the fourth quarter and were up $1 billion, or 1% from the previous quarter. Business lending achieved solid growth with adjusted balances totaling $52 billion at quarter end, an increase of 1%. Adjusted commercia l loans grew $563 million, or 1%. Commitments increased 2% and line utilization increased 30 basis points to 46.3%.

Consumer lending had another strong quarter, with every loan category increasing. Loans in this portfolio totaled $30 billion, an increase of 1% over the prior quarter. Indirect auto lending increased 2% and other indirect lending, which includes point of sale initiatives increased $55 million linked quarter, or 11%. We are pleased with the results of this new initiative. Year-to-date, loans in this portfolio have increased $339 million, and we expect continued growth in 2016. Looking at the credit card portfolio, balances increased 6% from the previous quarter, and our penetration rate into our deposit base now stands at 17.3%, up 160 basis points from the fourth quarter of last year. Mortgage loan balances increased $81 million and total home equity balances increased $31 million from the previous quarter as new production continued to outpace portfolio runoff.

Let's take a look at deposits. Average deposit balances increased $322 million, and ending balances increased over $1.2 billion during this quarter. Deposit costs remained at historically low levels at 11 basis points, and total funding costs remain low at 26 basis points. With respect to deposits, we are primarily core deposit-funded with 74% of our deposits coming from consumer and wealth deposits. Low-cost deposits were 92% of total deposits. Approximately half of our deposits come from cities with less than 1 million people, and 50% of our deposits are from customers with $250,000 or less in their account. This is why we believe our deposit base will be a competitive advantage for us as rates rise.

Now, let's look at how this impacted our results. Net interest income and other financing income on a fully taxable basis was $856 million, essentially flat with last quarter. However, excluding the impact of the lease adjustment, net interest income and other financing income increased $15 million, or 2%. Higher loan balances and balance sheet hedging and optimization strategies were the primary drivers behind the linked quarter increase along with interest recoveries. The benefit from interest recoveries is not expected to be at this level in the first quarter, approximately $4 million less going forward. The overall increase in net interest income and other financing income was partially offset by fixed asset repricing. The net interest margin was 3.08%. However, excluding the lease adjustment, net interest margin was 3.13%, or flat with the previous quarter.

Total non-interest income increased 4% on an adjusted basis from the third quarter, driven primarily by gains on sale of affordable housing investments and by higher card and ATM income. Card and ATM fees increased 3% primarily related to an increase in commercial bank card usage, and increase in a number of active cards of 3.7%, and an increase in seasonal consumer spending. Service charges were impacted by posting order changes that went into effect in early November and reduced non-interest income by approximately $7 million. We expect the ongoing impact of this change to be at the lower end of our previously stated $10 million to $15 million quarterly range. Wealth management income was down slightly quarter-over-quarter due to lower insurance income, partially offset by higher investment management and trust fee income. Capital markets income was relatively flat linked quarter as revenue from new product and service offerings was offset primarily by lower loan syndication fees.

Let's move on to expenses. Total reported expenses in the fourth quarter were $873 million. On an adjusted basis, expenses totaled $861 million, representing a decline of $33 million, or 4% from the prior quarter. This included a decrease of $24 million in FDIC fees primarily due to additional expenses of $23 million in the third quarter related to prior assessments. The expected quarterly run rate for this expense is in the $22 million to $24 million range excluding the impact of the proposed FDIC surcharge. Additionally, the fourth quarter benefited from lower expenses related to unfunded commitment costs of $12 million.

Salaries and benefits increased $8 million or 2% linked quarter, primarily attributable to $6 million in severance-related expenses. We also incurred $6 million of expenses related to 29 branch consolidations. Our adjusted efficiency ratio was 63.4% in the fourth quarter, but excluding the $15 million lease adjustment, the adjusted efficiency ratio was 62.7%. As discussed at Investor Day, we will continue to make investments to grow our business; however, we must be more efficient in everything we do. As Grayson noted, our plan to become a more efficient organization, including the elimination of $300 million in core expenses, is underway.

Let us move on to asset quality. Total net charge-offs increased $18 million to $78 million, and represented 38 basis points of average loans. This increase was primarily related to one large charge-off in the energy loan portfolio.

Total business services criticized and classified loans increased $117 million, driven by some weakening in a small number of larger loans primarily within the energy portfolio. However, total non-accrual loans, excluding loans held for sale, declined from the third quarter. Troubled debt restructured loans, or TDRs, also declined, down 1% from the prior quarter. The provision for loan losses was $69 million and our allowance for loan losses was down 2 basis points to 1.36% at the end of the fourth quarter. And at quarter end, our loan loss allowance to non-accrual loans or coverage ratio was 141%.

And regarding our energy portfolio, while oil prices have declined, exposure remains manageable. Should oil prices remain at current levels, charge-offs will be in the $50 million to $75 million range in 2016. The energy charge-off taken this quarter reduces the previous range of $50 million to $100 million. Additionally, we currently have just over $150 million reserved, or 6% of our direct energy exposure. And given where we are in the credit cycle, the volatility in certain credit metrics can be expected, especially related to larger dollar commercial credits in our portfolio and fluctuating commodity prices.

Let's move on to capital and liquidity. During 2015, we've returned $925 million to shareholders, which included the repurchase of $621 million of common stock and $304 million in dividends. And under Basel III, the Tier 1 ratio was estimated at 11.7% and the Common Equity Tier 1 ratio was estimated at 10.9%. On a fully phased-in basis, Common Equity Tier 1 was estimated at 10.7%, well above current regulatory minimums. Our loan and deposit ratio at the end of the quarter was 83%, and at the end of the quarter we were fully compliant as it relates to the liquidity coverage ratio.

Now let me give you an overview of our current expectations for 2016. We expect total loan growth to be in the 3% to 5% range on an average basis, excluding the impact of the operating lease reclassification. And regarding deposits, we expect full-year average deposit growth in the 2% to 4% range. And commensurate with our loan growth projections, we expect net interest income and other financing income to increase in the 2% to 4% range. Now, should we experience no additional rate increases, we expect to be at the lower end of that range.

As a result of our investments, we expect to grow adjusted non-interest income somewhere in the 4% to 6% range. And we will continue to make investments in 2016; however, we have also begun to execute our plan to eliminate $300 million of core expenses, of which 35% to 45% will occur in 2016. Therefore, we expect total adjusted non-interest expenses in 2016 to be flat to up modestly from 2015.

We expect to achieve an efficiency ratio of less than 63% in 2016 and positive operating leverage somewhere in the 2% to 4% range. And we still expect our net charge-offs to be in the 25 basis point to 35 basis point range. However, given the current price of oil, we would expect to be at the top end of that range.

In closing, the fourth quarter was a strong finish to a solid year. The investments we made in 2015 positions us well for 2016 and beyond. And we look forward to updating you on the progress throughout the year as we continue to build sustainable franchise value.

With that, we thank you for your time and attention this morning, and I will now turn it back over to List for instructions on the Q&A portion of the call.

M. List Underwood

Director of Investor Relations

Thank you, David. We are ready to begin, excuse me, the Q&A session of our call. In order to accommodate as many participants as possible this morning, I would like to ask each caller to please limit yourself to one primary question and one related follow-up question.

Now, let's open the line, operator, for your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. The floor is now open for questions. [Operator Instructions] We'll pause for just a moment to compile the Q&A roster. Your first question comes from Ryan Nash of Goldman Sachs.

Ryan M. Nash

Goldman Sachs & Co.

Q

Hey, good morning, guys.

O. B. Grayson Hall, Jr.

Chairman, President & Chief Executive Officer

A

Good morning, Ryan.

Ryan M. Nash

Goldman Sachs & Co.

Q

Maybe we'll just start off on credit, on first, can you maybe give us a little bit more color on the loss you took? What type of loan was it? Is there any credit left? And then, I guess when you think about the reserve that you've taken, the roughly 6%, what does your reserve contemplate for oil prices? And we've heard others say that if oil prices stayed at this level, you could see another incremental amount of provision. I'm just wondering what that number would be for you.

Barbara I. Godin

Chief Credit Officer & Senior Executive VP

A

It's Barb Godin, Ryan. Let me go ahead and answer that first part of the question.

Ryan M. Nash

Goldman Sachs & Co.

Q

Hi, Barb.

Barbara I. Godin
Chief Credit Officer & Senior Executive VP

A

And I'll address the second part. The first part was an energy credit that's been around for a few years. It was M&A activity, which originally led to the credit. It is a shared national credit. There're five banks involved in it. We saw some distress in this credit in the early part of the year. So we have been working this credit really hard during the course of the year. And it simply came to conclusion near the end of the year. And what we've done is we have appropriately marked that credit. We've taken the loss on that credit, as you've heard, and we've moved the residual balance into our held for sale. And we anticipate that we will have that out of our held for sale numbers by the end of, we're hoping, January, but certainly this quarter it will be out of your numbers. And back to individual credit, the charge off on that was approximately $25 million, adjust for rounding.

In terms of how we think about our reserve and look at prices as we work our way through our process, in the backs of our minds, we look at our price stack, our price stack is roughly $36 right now, sensitivity $28.90, so we're looking in that range as we determine and establish what those numbers should be. But we're also looking very heavily at each and every individual customer, what their cash flow looks like, what our collateral looks like, what our asset coverage is. We currently have asset coverage of 1.71 times on the [ph] ENT (23:58) book as an example. So, again, in conversations, and we had some ongoing conversations with our customers because we really do have a small number of customers, we still believe that repayment ability is adequate with them. And, again, establish our reserves accordingly.

Ryan M. Nash
Goldman Sachs & Co.

Q

Got it. And then, David commented in his prepared remarks that you're expecting charge offs to be towards the high end of the 25 to 35. I guess from both a portfolio, whether it's metals and minings or some other related areas, or even if it's across different geographies, whether it's Texas or Louisiana or anywhere else that's exposed to oil and gas. Are you seeing any other sort of changing in credit patterns, whether it ticks up in delinquencies or anything that's having impact on either growth or the overall credit performance?

Barbara I. Godin
Chief Credit Officer & Senior Executive VP

A

No, we're keeping a really close eye on all of that. There is some pressure, certainly, on commodities in general across the industry, as you know, and that's just given the strong U.S. dollar, what's going on in Europe and in China in terms of the dislocation of the markets. So there is some pressure there, but we've seen nothing yet that is significantly concerning.

Ryan M. Nash
Goldman Sachs & Co.

Q

All right, maybe one, just one last quick one. David just can you help us understand the trajectory of the net interest margin? I guess maybe both based on the forward curve and if we don't get any additional rate hikes in 2016, where do you think the NIM would trend over the course of the year?

David J. Turner, Jr.
Chief Financial Officer & Senior Executive Vice President

A

Yeah, so, Ryan, I gave a little bit of guidance in terms of if we don't get another change, we'll be at the lower end of our 2% to 4% guidance that we've given you. I also gave you a little bit of guidance in my prepared comments in terms of barge and we did have unusual interest recoveries. We think about $4 million of that won't repeat going forward. But we're looking for a relatively stable NIM. And this is adjusting, by the way, for the lease accounting, so we were at 3.08 on net interest margin, five points related to lease adjustments, so 3.13 would have made us flat and we're looking for a relatively stable – and just to remind everybody, that's been one or two points either side of where we are for 2016. And so we're looking for that guidance in terms of growth in NII that we've really been focusing on to be that 2% to 4% through the year. So you may see some unusual changes in a given quarter, but you've got to keep the year in mind when thinking about NIIs or trajectory.

Ryan M. Nash
Goldman Sachs & Co.
Q

Got it. Thanks for taking my questions.

Operator: Your next question comes from David Eads of UBS.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer
A

Morning, Dave.

David Eads
UBS Securities LLC
Q

Hi, good morning. Maybe following up on energy. When I look at the – you guys had some disclosure on the criticized loans, which I thought was pretty interesting. And when you look at it, the criticized loans are actually higher on a percentage basis in the E&P portfolio compared to the oil field services. So I was wondering if you could just talk a little bit about what you're seeing that – has you more comfortable with the exposures on the E&P side and I guess maybe a little bit less so on the oil field services.

Barbara I. Godin
Chief Credit Officer & Senior Executive VP
A

Again, it's Barb Godin, I'll be happy to answer that. As we do our redeterminations, and we've just finished up our fall redeterminations, just about done. What happens is as you readjust the borrowing base and, again, for fall redeterminations this year borrowing base adjustments downwards were a little under 8%, notwithstanding if that causes an over advance. What we will immediately do is call that loan a criticized loan and move it into a non-pass category. So again, that would account for the reason that we have roughly 48% of our E&P book that is shown right now as criticized. Having said that, we have a rigorous process, as well, around our oilfield services portfolio. As you can see on the charts that we did provide, 32 customers make up 75% of that portfolio. So we're able stay in constant and close contact with them. Again, if we see any weakness there, again, we are very quick to move it into a criticized category.

David Eads
UBS Securities LLC
Q

Just maybe to follow-up on that, on the E&P portfolio, if you have 400 – if close to half of the loans were in – a lot of those were in an over-advanced positions, I would think that they'd only be in a further over-advanced position now where oil prices have gone since the redetermination was complete. So would that suggest that criticized loans are – the real criticized exposure might even be higher than that?

Barbara I. Godin
Chief Credit Officer & Senior Executive VP
A

No. If I take the spring redetermination that we did, that was somewhere between – let's just use roughly 15% reduction and borrowing basis. And now we're seeing that there's an incremental 8%, I'll round it up, on top of that, so roughly 23% reduction in borrowing base. Remember, as well, in the industry customers get a six-month cure period in which they're able to cure, and we have seen a number of customers – again those earlier in the year that had access to capital markets and even now those that are still very strong, some of them have access to capital markets and they're able to take themselves out of an over-advanced position.

David Eads
UBS Securities LLC
Q

Okay. And then maybe just as we think about the dislocations we're seeing in the markets right now, I know it's fairly early, but do you guys have any sense of how that – if this continues, how that would impact the strategy you guys have for growing the capital markets and wealth management business? Is there anything that's particularly sensitive to market activity levels and that you'd be more concerned about the growth trajectory?

David J. Turner, Jr.
Chief Financial Officer & Senior Executive Vice President
A

This is David. I will tell you that we are creating these new products and services. The driver of that is because our customers need that and we're looking to have a more fulsome offering to our customers and we're out there talking to them and feel very good about where they stand right now, which is why I reiterated our guidance for 2016 on things like loan growth being in the 3% to 5%. We're seeing in our discussions with our customers, we still see the domestic economy being okay. We're looking at 2%, 2.5% GDP. And so there is this dislocation that's happening here of late, but as we see our customers, we believe they need the products and services, the capital markets investments we make and we think are going to be very strong and looking for that to continue and help us get to that 4% to 6% growth rate that we're expecting in non-interest revenue.

David Eads
UBS Securities LLC
Q

Great. Thanks for taking my questions.

Operator: Your next question comes from John Pancari of Evercore ISI.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer
A

Hey, John.

Stephen Moss
Evercore Group L.L.C.
Q

Hey, good morning. It's actually Steve Moss for John. How are you all doing?

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer
A

Good morning, Steve. Doing well.

Stephen Moss
Evercore Group L.L.C.
Q

I guess first off for List, congratulations and good luck on your retirement here.

M. List Underwood
Director of Investor Relations

A

Thank you, thank you.

Stephen Moss
Evercore Group L.L.C.

Q

And I wanted to ask about energy again. Just wondering here with regard to oil, if declines further to $20 to $25, let's say, what are your potential losses there?

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer

A

Well, as we look at – and I'll ask Barb to reiterate and complete the statement, but we look at our energy portfolio. We have got a very disciplined process of calculating probability to faults and loss given to faults. We've got the redeterminations that we're doing on E&P portfolio twice a year and so we feel good about th e level of rigor and discipline around our process that drives that evaluation of how much we reserve based on what we think the incurred losses may be. And so I think our confidence in that process is very solid. We're staying disciplined around that process. And if oil prices continue to decline, that process is going to drive risk ratings down on some of our credits. It will drive a higher level of criticized classified loans and it will drive how we reserve against those loans. But it will be on an incurred loss basis and until that incurred loss occurs, from an accounting perspective, our process is going to determine that. So, Barb? Do you want to add to it?

Barbara I. Godin
Chief Credit Officer & Senior Executive VP

A

I think what I would add to that is the operative word here being how long will oil prices stay depressed. You mentioned somewhere in the $20 a barrel range and again, if it's in the $20 a barrel range and it stays there for an entire year, it could be, in terms of charge offs, since it's not in provision, could be up to an incremental $50 million. And that is based on some back of the envelope versus anything precise, I would have to tell you. But again, that's not our view and I don't think it's the view of the industry at this point that oil is going to stay sub-$30 for any length of time.

Stephen Moss
Evercore Group L.L.C.

Q

Okay. And then with regard to the criticized level, you indicated on E&P it was 48%, I was just wondering what is the total amount of criticized loans in the energy portfolio?

Barbara I. Godin
Chief Credit Officer & Senior Executive VP

A

The total amount of criticized loans in terms of everything including the operating leases we had, $900 million.

Stephen Moss
Evercore Group L.L.C.

Q

Yes. Okay.

Barbara I. Godin
Chief Credit Officer & Senior Executive VP

A

$900 million on 3.2, or 28%.

Stephen Moss
Evercore Group L.L.C.

Q

Great. And then I guess one more thing. With regard to the margin, just a little more color here in terms of short-term expectations for the margin. Given the first Fed hike, how would you think about the margin in the first quarter?

David J. Turner, Jr.
Chief Financial Officer & Senior Executive Vice President

A

Yeah, so I tried to give you a little bit more global view of where we thought NII and margin was going. So when we start breaking it down, we get pretty granular. There's puts and takes either way. If you just want to focus on that component of the December increase, we're probably benefiting in the $5 million to $10 million range in the first quarter. But remember there are some other things going the other way. You've got day counts about $5 million dollars working against you, you've got the interest reversal of $4 million that I talked about in my prepared comments. So I think it's better to kind of look overall at the guidance in terms of relatively stable margin, and growth in NII in that 2% to 4% range commensurate with the loan growth that we've talked about of 3% to 5%.

Stephen Moss
Evercore Group L.L.C.

Q

Okay. Thank you very much.

Operator: Your next question comes from Geoffrey Elliott of Autonomous Research.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer

A

Good morning, Geoffrey.

Geoff Elliott
Autonomous Research LLP

Q

Good morning. Congratulations to List on your retirement. So on energy again, looking at the build from 4.7% reserves that you talked about at the Investor Day for 3Q up to the 6% and then taking into account the charge offs as well, to me it looks like almost all of the provisioning in the quarter related to the energy portfolio. Is that the right way to be thinking about it, or am I missing something there?

Barbara I. Godin
Chief Credit Officer & Senior Executive VP

A

No, you're actually thinking about it right. If you look at the balance of our book, the balance of our book actually improved. And we were able to reallocate that provision over to the energy sector.

Geoff Elliott
Autonomous Research LLP

Q

Great.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer

A

And if you look at the credit quality of our book and you ex energy, then the balance of our book performed very well this past quarter. And we continue to see improvements in almost all of our credit metrics. But if you loo k at, if you add the energy back in, and to Barb's point, there's stress in that sector. But because the way our portfolio's performing, it allowed us to build reserves around the energy portfolio.

Geoff Elliott
Autonomous Research LLP
Q

Great. That's clear. And then just to follow up, you've mentioned commodities a couple of times in the discussion. Can you just remind us where the other commodities exposures are and how stress in commodities beyond oil and gas could have some impact on credit?

Barbara I. Godin
Chief Credit Officer & Senior Executive VP
A

As I think about commodities, firstly, our [ph] book-in (36:40) commodities, we have roughly $400 million in fabricated metals, and primary metals, another $430 million. So just to give you a rough sense for the size of the book. And again, a lot of those commodities in terms of metals, that's also an indirect hit, so to speak, from what's happening in the oil sector. Because they rely on a lot of those metals to provide piping, et cetera. And so tha t's where we're seeing a secondary knock on effect and one that we're keeping a close eye on.

Geoff Elliott
Autonomous Research LLP
Q

Great. Thank you very much. Oops, sorry.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer
A

Oh, and I said, we have a fairly minor exposure to agriculture.

Barbara I. Godin
Chief Credit Officer & Senior Executive VP
A

Yes, $800 million in ag.

Geoff Elliott
Autonomous Research LLP
Q

Thank you.

Operator: Your next question comes from Stephen Scouten of Sandler O'Neill.

Stephen Kendall Scouten
Sandler O'Neill & Partners LP
Q

Hey, thanks, guys.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer
A

Hey, Stephen.

Stephen Kendall Scouten
Sandler O'Neill & Partners LP

Q

Question for you maybe on the expenses. You had some nice progress here in the quarter. I'm wondering, is any of that going to reverse out in the coming quarter especially maybe that $12 million on the unfunded commitments that was saved? And maybe beyond that, are you still expecting about 35% to 45% of the $300 million in saves to come out here in 2016?

David J. Turner, Jr.
Chief Financial Officer & Senior Executive Vice President

A

So we do expect 35% to 45% of the $300 million to come out in 2016. And you're right that the unfunded, the reason we worked that out separately is that, that is not something that is expected to benefit, at least to the degree we had in the second quarter. So we want to call it out separately so you could take that into acc ount in your model.

Stephen Kendall Scouten
Sandler O'Neill & Partners LP

Q

Okay. And just on a net basis, do you still believe that the $300 million really just allows you to keep overall expenses relatively flat and maybe even still up on a total dollar amount for 2016?

David J. Turner, Jr.
Chief Financial Officer & Senior Executive Vice President

A

Yeah, that's right, Stephen. We're calling for continuing to make investments to grow NIR, utilizing our savings of the $300 million, at least a 35% to 45% of that, to help us keep expenses relatively flat to up modestly from that level that we're reporting for 2015.

Stephen Kendall Scouten
Sandler O'Neill & Partners LP

Q

Okay, great. And then maybe if I could on capital and the buyback. It seems like you got about $350 million remaining maybe relative to the CCAR ask. Could that be accelerated in the quarter based on where the stock is trading now, with it under tangible book? Is that something where you guys can take advantage of where the stock is trading currently?

David J. Turner, Jr.
Chief Financial Officer & Senior Executive Vice President

A

So any change to – so the $350 million is right. $175 million generally in each quarter. In order to change the amount and/or timing requires an approval from our regulatory supervisors, and there is a mechanism for doing that. But we have to assess that and can't guarantee there would be any change from what's already been approved.

Stephen Kendall Scouten
Sandler O'Neill & Partners LP

Q

Okay. Thanks for the color, guys. I appreciate it.

Operator: Your next question comes from Gerard Cassidy of RBC.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer

A

Hey, Gerard, good morning.

John Hearn
RBC Capital Markets LLC

Q

Hey, good morning, guys. This is actually John Hearn on for Gerard. Just two questions for you. The first back to the criticized balance for the energy portfolio, can you tell us what it was in the third quarter?

Barbara I. Godin
Chief Credit Officer & Senior Executive VP

A

Criticized balance, it was roughly $300 million less.

John Hearn
RBC Capital Markets LLC

Q

$300 million less. Okay.

Barbara I. Godin
Chief Credit Officer & Senior Executive VP

A

I can get you an exact number after the call.

John Hearn
RBC Capital Markets LLC

Q

All right, thank you. And then more broadly, the regulators in December, I believe, they expressed some concern about underwriting standards for CRE and construction lending. Can you comment a bit about what you're seeing in those segments? And are you beginning to see any changes since the comments came out?

Barbara I. Godin
Chief Credit Officer & Senior Executive VP

A

No, in fact, we're feeling very good about our book, CRE and construction lending, back to, we used to have a book that was very heavy. Previously going back several years and we've taken a lot of lessons from that to ensure that we understand what we're putting on our books and that we need to feel comfortable both in a stress situation as well as a normal situation. So we have been very deliberate about what we are putting on the books. We have not had very much growth, came off a very low base in terms of growing that book. And, again, very deliberate on the types of credits that we're willing to underwrite. So again, from a credit perspective, I feel very comfortable.

John Hearn
RBC Capital Markets LLC

Q

All right, excellent. Thanks for taking the questions. Appreciate it.

Operator: Your next question comes from Christopher Marinac of FIG Partners.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer

A

Good morning. Chris.

Christopher William Marinac
FIG Partners LLC
Q

Thanks, good morning. Hey, good morning. I just wanted to ask about where acquisitions may fit in, in select markets if at all this next year?

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer
A

Yeah, I mean, Chris, we certainly are very analytical and disciplined about how we focused on acquisitions, quite frankly. Our primary focus has been on bolt on acquisitions in the non-bank space. In 2015, we did two relatively small transactions that you're familiar with. We continue to look at the marketplace, and we still think there's opportunities in both our wealth segment as well as our capital markets segment, and insurance segments for bolt on acquisitions. We continue to look. I think that the expectation is these are going to be relatively small in size and still at this juncture we're – evaluations are that predominantly our interest is in the non-bank space.

Christopher William Marinac
FIG Partners LLC
Q

Okay. Great, thanks for that color. And, Grayson, if pricing did change, would you reconsider the bank's odd, or would that have to shift a lot to affect that?

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer
A

As markets change, we always reconsider. So markets change, we try to analyze what the changes are and see where the opportunities are.

Christopher William Marinac
FIG Partners LLC
Q

Okay. Very good. Thanks so much.

Operator: Your next question comes from Peter Winter of Sterne Agee.

Peter J. Winter
CRT Capital Group LLC
Q

Good morning.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer
A

Good morning.

Peter J. Winter
CRT Capital Group LLC
Q

I just want to go back to the 2016 expectations, the operating leverage of 2% to 4%. If the revenues come in a little bit weaker than expected, would you guys let more of the expenses fall to the bottom line to ensure that operating leverage that you're forecasting?

David J. Turner, Jr.
Chief Financial Officer & Senior Executive Vice President
A

Yeah, we've looked at a lot of different scenarios, Peter, in terms of committing to the 2% to 4%, or at least indicating that we could get to 2% to 4% operating leverage. There are a lot of different scenarios. We believe through our expectations of revenue growth and our expectations of expense management, that we'll get there. Now the combination of how we get there may change, and we'll adjust, adapt, and overcome. But our goal is to generate that positive operating leverage regardless of the environment.

Peter J. Winter
CRT Capital Group LLC
Q

Got it. Thanks very much. And congrats, List, on the retirement.

M. List Underwood
Director of Investor Relations
A

Thanks, Peter.

Operator: Your next question comes from Jack Micenko of SIG.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer
A

Good morning, Jack.

Jack Micenko
Susquehanna Financial Group LLLP
Q

Hi, good morning. One of the industry conferences in the fourth quarter, I think you had disclosed that you were moving towards the upper end on the branch closure range that you gave at Investor Day. Does that still hold true? And then the second question would be the cadence of those closures, should we think about – is there any kind of guidance we can think about in dealing with modeling some of those one-time charges that we saw, like, in this quarter?

David J. Turner, Jr.
Chief Financial Officer & Senior Executive Vice President
A

Yeah, Jack, so we did say we were looking at 100 to 150 branches. We said we would probably be towards the upper end of that through our strategic planning period. We've announced 29. We continue to look each and every day at how to best optimize our branch footprint, which has included even growing some, or opening some new ones at times. But it's hard to get the cadence down to give you that commitment upfront because it's all fact and circumstances based. We have to look at our footprint, what's going on in the footprint. We have a lot of coordination that has to happen.

What I can tell you is, so we had a $6 million charge on the 29 branches that we closed, or made a decision on consolidating this quarter. There will be another roughly $6 million associated with those branches. So it's, call it, $12 million. And we expect a payback on that of about two years, which is what we've had historically. So all branches aren't created equal, they're all a little different. But if you go back and look at all of our branch consolidations, it will give you a feel for what that charge might be over time. But it's hard for me to give you the precise timing.

Jack Micenko
Susquehanna Financial Group LLLP

Q

Okay, thank you. And then, obviously, you have a large – large portion of your deposits are consumer. Have you been feeling any pressure on the commercial side to pass on any of the rate increase some of the other banks have talked about it today?

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer

A

No, at this juncture, we just have not seen deposit rate pressures. Given such a fairly modest increase in rates, the pressure from any part of our depository base has been very muted. We continue to watch very closely what our competitors are and watch very closely what our customers are saying to us. But quite to the contrary, we continue, as you saw this quarter, to grow deposits and, in fact, grow low-cost deposits at a pretty healthy pace, and so we're just not seeing that particular issue arise at this juncture.

Jack Micenko
Susquehanna Financial Group LLLP

Q

All right, thank you.

Operator: Your next question comes from Kevin Barker of Piper Jaffray.

M. List Underwood
Director of Investor Relations

A

Good morning, Kevin.

Kevin J. Barker
Piper Jaffray & Co (Broker)

Q

Hello, good morning. You made the comments that you're looking at acquisitions in the non-bank space. Could you describe that a little bit further and what targets you're looking at potentially in order to expand your fee income?

M. List Underwood
Director of Investor Relations

A

Go ahead.

David J. Turner, Jr.
Chief Financial Officer & Senior Executive Vice President

A

Sure, this is David. So as Grayson mentioned, we really – one of our strategic initiatives is to diversify our revenue. And in this context, diversification is a way from NII and into NIR. As we think about the desire to diversify and we think about how we can have a more fulsome offering to our customers, things in capital markets have come to mind. So you saw our acquisition of BlackArch Partners, our M&A advisory firm. We've looked at insurance entities and we'll continue to do that agencies, continue to expand there. We would like to have a more solid offering in fixed income sales and trading, so we're looking there. And I think that these acquisitions have a tendency to be smaller acquisitions, but they fit into our need and our desire to continue to diversify, and we think fit very well with our strategy.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer

A

And really serve the customer need. When you're trying to identify the needs that our customers have and how we can serve those better, but at the same time, to David's point, diversify our revenue. But we make sure that these are incremental in nature, bolt-on acquisitions that don't – that have a risk profile that we feel like is prudent. And so I think you can see us – you should expect us to continue to look at those opportunities over 2016. But our primary focus, as you've seen, is on organic growth in the markets we're in today, with the services we have today, but this is in addition to that. But primary focus is organic growth.

Kevin J. Barker
Piper Jaffray & Co (Broker)

Q

Okay. And my apologies if somebody might have mentioned this earlier, but in regards to your CCAR in 2016, you had a pretty big impact from the stress test last year. Given the decline in oil prices and where you are now, do you anticipate a similar decline this time around, and how are you preparing for CCAR going into 2016?

David J. Turner, Jr.
Chief Financial Officer & Senior Executive Vice President

A

Well, so we've got a lot of work going on with CCAR to be prepared for our submission in April. We look at a lot of different portfolios. I think from a credit standpoint, we mentioned earlier that ex energy, our credit portfolios are actually improving. And so that works one way in terms of the CCAR submission. Energy clearly needs to be taken into account, and I think Barb laid out some of the stresses that we're seeing and how we'll account for those.

So, from our standpoint, we have one of the strongest levels of Common Equity Tier 1 of our peer group. We did return 93% of our earnings to our shareholders, which we think was appropriate. And as a result, we didn't want to continue to accrete capital because we felt like we had enough capital to run our business in a prudent manner. So we look at our stresses all the time, not just from a CCAR standpoint, we do that for ourselves to make sure we're managing and optimizing our capital in our company so that we have enough in time to stress, and – but not too much in terms of ensuring we can have an appropriate return to our shareholders. So exactly how all this will manifest itself in CCAR, we'll have to see and let the – we run a lot of programs. We'll just need to see what the results are. We don't see anything drastically different than what we have submitted before ex energy.

Kevin J. Barker
Piper Jaffray & Co (Broker)

Q

Okay. Thank you for taking my questions.

Operator: Your final question comes from Stephen Scouten of Sandler O'Neill.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer

A

Hey, Stephen, good morning.

Stephen Kendall Scouten
Sandler O'Neill & Partners LP

Q

Hey, thanks for letting me hop on for one follow-up. I just wanted to confirm that $50 million to $75 million in potential incremental [ph] off if the oil (51:18) stays around here. That's assumed just for 2016 as I heard it, and so would we assume that there could be further tail risk if oil prices remain depressed for a longer period of time?

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer

A

That's right. That's a 2016 number, and obviously if oil stays low longer, then there is tail risk to that.

Stephen Kendall Scouten
Sandler O'Neill & Partners LP

Q

Okay. Thanks so much, guys. Congrats on the good operating quarter.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer

A

Thank you.

O. B. Grayson Hall, Jr.
Chairman, President & Chief Executive Officer

Well, with that, we stand adjourned. Thank you for your participation and we look forward to the next quarter. Thank you.

Operator: Thank you. This concludes today's conference call. You may now disconnect.

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