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CORPORATE PARTICIPANTS

Dana W. Nolan
Executive Vice President - Head of Investor Relations, Regions Financial Corp.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

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

John Turner
Senior Executive Vice President-Head of Corporate Banking Group, Regions Financial Corp.

Barbara I. Godin
Chief Credit Officer & Senior Executive Vice President, Regions Financial Corp.

OTHER PARTICIPANTS

Matthew Hart Burnell
Analyst, Wells Fargo Securities LLC

Michael Rose
Analyst, Raymond James & Associates, Inc.

Elizabeth Lynn Graseck
Analyst, Morgan Stanley & Co. LLC

John Pancari
Analyst, Evercore ISI

John Eamon McDonald
Analyst, Sanford C. Bernstein & Co. LLC

Geoffrey Elliott
Analyst, Autonomous Research LLP

Kenneth M. Usdin
Analyst, Jefferies LLC

Robert F. Placet
Analyst, Deutsche Bank Securities, Inc.

Steve Moss
Analyst, FBR Capital Markets & Co.

Saul Martinez
Analyst, UBS Securities LLC

Gerard Cassidy
Analyst, RBC Capital Markets LLC

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 participant 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 Ms. Dana Nolan to begin.

Dana W. Nolan

Executive Vice President - Head of Investor Relations, Regions Financial Corp.

Thank you, Paula. Good morning and welcome to Regions' fourth quarter 2016 earnings conference call. Participating on the call are Grayson Hall, Chief Executive Office; and David Turner, Chief Financial Officer. Other members of senior management are also present and available to answer questions.

A copy of the slide presentation referenced throughout this call, as well as our earnings release and earnings supplement, are available under the Investor Relations section at regions.com.

I'd also like to caution you that we will make forward-looking statements during today's call that are subject to risk and uncertainties, and we'll also refer to non-GAAP financial measures. Factors that may cause actual results to differ materially from expectations, as well as GAAP to non-GAAP reconciliations, are detailed in our SEC filings.

I will now turn the call over to Grayson.

O. B. Grayson Hall

Chairman, President & Chief Executive Officer, Regions Financial Corp.

Thank you, Dana, and good morning. Thank you for joining our call today. I'll review highlights for our full year financial performance, and David will cover the results for the fourth quarter specifically. Let me begin by saying that we're very pleased with 2016 results. We diligently executed our strategic plan and maintained our focus on our business fundamentals.

Central to our success has been the continued emphasis on three strategic initiatives; growing and diversifying revenue, practicing disciplined expense management, and effectively deploying our capital. Net income available to common shareholders for 2016 was $1.1 billion, a 10% increase over 2015. Earnings per share was $0.87, representing a 16% increase over the prior year. Total taxable equivalent revenue grew 3%, and reported non-interest expenses were relatively flat.

In late 2015, we laid out financial targets for 2016. Although, the operating environment proved somewhat more challenging than anticipated, [ph] or forecasted, (02:30) we still met or exceeded most of our performance targets.

For example, we grew net interest income 3% versus the prior year. We also grew adjusted non-interest income 7%, driven by growth in customer relationships and new product offerings. For example, through new enhanced products and capabilities, capital markets income increased 46% in 2016, and wealth management income increased 6%.

Adjusted non-interest expenses increased just under 2%, in line with our target of flat to up modestly. Importantly, we generated positive operating leverage, which is a critical metric and part of our focus to the adjusted basis of 3%. And the adjusted full-year efficiency ratio was 63.3%.

Finally, full year net charge-offs totaled 34 basis points. Regarding loan growth, 2016 presented some unique challenges, which we tackled head on, and we were intentional and thoughtful in how we managed our portfolio. Average loans were relatively stable in the fourth quarter of 2016 as compared to the prior year.

Notably, the overall financial health of our consumer portfolio was strong, and we saw solid demand and steady loan growth in almost all consumer loan categories. Average consumer loans grew $1.2 billion or 4% from the fourth quarter of prior year.

On the other hand, average business lending balances declined 3% from the fourth quarter of prior year. This decline was driven by our continued focus and a thoughtful focus on achieving appropriate risk-adjusted returns, the de-risking of certain portfolios and asset classes and the ongoing softness in demand for middle market, commercial and small business loans.

Looking ahead, we are encouraged by recent increases in market interest rates, as well as possible benefits associated with the new administration. We remain focused on improving efficiencies. Our plan to eliminate $400 million of core expenses through 2019 remains firmly intact. This along with our continued focus on appropriate risk-adjusted returns are fundamental to our long-term success and sustainability of our franchise value.

With respect to capital deployment, we remain committed to effectively deploying our capital through organic growth and strategic investments that increase revenue or reduce ongoing expenses, while returning an appropriate amount of capital to shareholders.

During 2016, we returned $1.2 billion of our earnings to shareholders through a combination of dividends and share repurchases, while at the same time, maintaining robust and industry-leading capital levels.

On a separate note, we are pleased that our satisfactory CRA rating has been reinstated. We remain committed to optimizing our branch network, and we'll optimistically expand [ph] into select (05:28) growth markets.

During 2016, we consolidated 103 branches and announced plans to consolidate another 23 offices. As previously announced, our plan is to consolidate at least 150 branch offices by the end of 2017.

In closing, I want to thank our team of 22,000 associates for their hard work and dedication in delivering solid financial results and their continued commitment to superior customer service. We're extremely proud of our accomplishment in 2016, are well-positioned to build on that momentum in 2017.

With that, I'll turn it over to David to cover the specific details of the fourth quarter. David?

David J. Turner, Jr.

Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.

Thank you, Grayson, and good morning, everyone. Let's get started with the balance sheet and look at average loans.

In the fourth quarter, average loan balances totaled $80.6 billion, down 1% from the previous quarter and relatively flat with the fourth quarter of 2015. Consumer lending remains a positive story for us, as we experienced another quarter of solid growth. Average balances increased $329 million, or 1%, over the prior quarter and $1.2 billion, or 4%, over the prior year. This growth was led by mortgage lending, as balances increased $236 million, or 2%, linked quarter and $732 million, or 6%, over the same quarter of the prior year.

We made the decision to sell $171 million of affordable housing residential mortgage loans to Freddie Mac during the fourth quarter and generated a gain of $5 million. Approximately $91 million of these loans included recourse and will remain in loans held for sale at yearend until the recourse expires later in 2017. Subsequent to the expiration of recourse provisions, it is expected that an additional $5 million gain will be recognized. The economics of the transaction and improved diversification drove the decision to sell.

We continue to experience success with our other indirect lending portfolio, which includes point-of-sale initiatives. This portfolio increased $110 million, or 14%, linked quarter and $366 million, or 70%, year-over-year. Average balances in our consumer credit card portfolio increased $36 million, or 3%, over the prior quarter and $115 million, or 11%, over the fourth quarter of 2015. Penetration into our existing deposit customer base increased to 18.4%, an improvement of 110 basis points year-over-year.

Turning to the indirect auto portfolio, average balances decreased $17 million during the quarter. As previously disclosed, we terminated a third-party arrangement during the fourth quarter that historically accounted for approximately one-half of our total indirect vehicle production. As such, we expect the pace of run-off in the portfolio to exceed production generated by our preferred dealer network. Average home equity balances also decreased $64 million, as the pace of run-off exceeded production.

Now turning to business lending, average balances decreased $1 billion, or 2%, during the quarter and $1.4 billion, or 3%, year-over-year. As Grayson mentioned, the decline in business lending balances was impacted by our continued focus on achieving appropriate balance and diversity, while also improving risk-adjusted returns. Importantly, balances reflect decisions and choices that we made during the year. We continue to reduce exposure due to concerns about increasing risk in certain industries and asset classes.

Average direct energy loans decreased $491 million, or 19%, and average multi-family loans decreased $239 million, or 12%, compared to the fourth quarter of 2015. Further, continued softness in demand and increasing competition for middle market and small business loans has also impacted loan production.

While there have been headwinds to business lending growth in 2016, we continue to expect low-single-digit average loan growth in 2017. Areas within business lending expected to contribute to this growth include technology and defense, healthcare, power and utilities, and asset-based lending.

So let's start with deposits. Total average deposit balances increased $561million from the previous quarter and $1 billion year-over-year. Average low-cost deposits increased $503 million and $1.3 billion over the same respective periods. Deposit costs remain near historically low levels at 13 basis points, and total funding costs remained low, totaling 30 basis points in the quarter.

Total average deposits in the Consumer segment were up $452 million, or 1%, in the quarter and $2.7 billion, or 5%, year-over-year. This growth reflects the unique strength of our retail franchise, the overall health of the consumer, and our ability to grow low-cost deposits.

Average Corporate segment deposits increased $437 million, or 2%, during the quarter and $1.2 billion, or 4%, year-over-year, as corporate customers remained focused on liquidity. Average deposits in the Wealth Management segment decreased $398 million, or 4%, during the quarter and $2.3 billion, or 18%, year-over-year.

Certain institutional and corporate trust customer deposits, which require collateralization by securities, continue to shift out of deposits and into other fee income-producing customer investments. So let's look at how this impacted our results.

Net interest income and other financing income on a fully taxable basis was $874 million in the fourth quarter, an increase of $18 million, or 2%, from the third quarter. The resulting net interest margin was 3.16%, an increase of 10 basis points. Both net interest margin and net interest income and other financing income benefited from several factors during the quarter, including higher interest rates, lower premium amortization on investment securities, a leveraged lease residual value adjustment incurred in the third quarter that did not repeat, and higher security balances. These increases were partially offset by lower loan balances. Net interest margin also benefited from lower average cash balances held at the Federal Reserve.

The increase in interest rates during the quarter reduced the amount of the premium amortization on mortgage-related securities to $43 million from $49 million, and premium amortization is expected to decline further in the first quarter of 2017. Now, if interest rates remain at current levels, or continue to rise, we would expect to benefit from marginal declines in premium amortization ultimately achieving a quarterly run rate in the low to mid $30 million range in 2017.

Non-interest income decreased 13% in the quarter, primarily due to insurance proceeds related to the FHA settlement recognized in the third quarter. Non-interest income increased $8 million, or 2%, compared to the fourth quarter of 2015. Adjusted non-interest income decreased 6% in the quarter, but increased 2% year-over-year. Service charges increased 4% in the quarter. However, this growth was more than offset by declines in capital markets, wealth management, mortgage, and other non-interest income.

Following a record third quarter, capital markets income decreased $11 million, or 26%, during the quarter, driven primarily by lower merger and acquisition advisory services. Capital markets income increased $3 million, or 11%, compared to the fourth quarter of 2015, driven by increased debt underwriting activity.

Also coming off a record third quarter, wealth management income decreased $4 million, or 4%, as lower insurance and investment services income were only partially offset by higher investment management and trust fees. Compared to the fourth quarter of 2015, wealth management income increased $3 million, or 3%, as growth in investment management and trust fees exceeded the decline in investment services, while insurance income was unchanged.

Mortgage income decreased $3 million, or 7%, driven by seasonally lower production, partially offset by increases in the market valuation of mortgage servicing rights and related hedging activity. Within total mortgage production, 59% was related to purchase activity and 41% were related to refinancing. Mortgage income increased 16% compared to the fourth quarter of 2015, primarily due to increased gains associated with a 29% increase in production.

Also during the quarter, we completed another bulk purchase of the rights to service approximately $2.2 billion of mortgage loans. This brings our total purchases for 2016 to approximately $8.1 billion and our mortgage servicing portfolio has increased $6 billion to $45 billion. Mortgage servicing income increased $5 million, or 6%, in 2016 compared to 2015. We still have capacity and we'll continue to evaluate opportunities to grow our servicing portfolio.

And finally, other non-interest income declined during the quarter, as the company recognized the recovery during the third quarter of approximately $10 million related to the 2010 Gulf of Mexico oil spill, which did not repeat this quarter.

So let's talk about expenses. Total non-interest expenses decreased 4% during the quarter. On an adjusted basis, expenses totaled $877 million, also representing a 4% decrease quarter-over-quarter, reflecting the results of our efficiency initiatives.

Total salaries and benefits decreased $14 million from the third quarter, primarily due to a decline in base salaries associated with one less weekday, the impact of staffing reductions, and lower production-based incentives related to decreased capital markets and commercial banking production. Staffing levels continued to decline during the quarter and decreased 5%, or over 1,200 positions, in 2016, as we executed on our efficiency initiatives.

Professional and legal expenses decreased $3 million during the quarter, primarily due to lower litigation-related costs. We also recognized an $11 million linked quarter benefit associated with the credit for unfunded commitments. And finally, recall, there was an $11 million expense in the third quarter associated with Visa class B shares that did not repeat in the fourth quarter.

The fourth quarter adjusted efficiency ratio was 63.2%. And as Grayson mentioned, we remain committed to achieving our expense elimination plans and our long-term target for an adjusted efficiency ratio below 60% by 2018. The company's effective tax rate for the fourth quarter and full year 2016 was 31.2% and 30.7%, respectively. And the effective tax rate is expected to be in the 30% to 32% range for the full year 2017.

Let's move on to asset quality. Net charge-offs totaled $83 million in the fourth quarter, an increase of $29 million from the third quarter and represented 41 basis points of average loans. Charge-offs related to our direct energy portfolio totaled $14 million in the quarter.

The provision for loan losses was $35 million less than net charge-offs, and our allowance for loan losses as a percent of total loans decreased 3 basis points to 1.36%. The allowance for loan and lease losses associated with the direct energy loan portfolio decreased to 7% in the fourth quarter compared to 7.9% in the third quarter, which reflects continued improvement in credit quality of the energy book, and our exposure to direct energy continued to decline, ending the year at 2.6% of total loans outstanding.

Total non-accrual loans, excluding loans held for sale, decreased 9 basis points to 1.24% of loans outstanding, and total business services criticized loans decreased 3%. The improvement in business services criticized loans was primarily due to declines in energy and energy-related credits. The improvement in non-accrual loans was driven by declines in non-energy commercial loans.

Troubled debt restructured loans increased 5% in the quarter, primarily due to increases in indirect energy credits. Allowance for loan losses as a percentage of total non-accrual loans or coverage ratio was 110% at quarter-end. Excluding energy, the coverage ratio increased from 123% to 138% in the fourth quarter. Direct energy charge-offs totaled $37 million in 2016 and are expected to be less than $40 million in 2017, given current market conditions

And under our stress scenario, with oil averaging below $25 per barrel, incremental losses could total $100 million over the next eight quarters. We are encouraged by the performance of our energy portfolio to-date. However, we will continue to monitor and manage it closely. Given where we are in the credit cycle and considering fluctuating commodity prices, volatility in certain credit metrics can be expected, especially related to larger dollar commercial credits.

Let's talk about capital and liquidity. As Grayson mentioned, we returned $1.2 billion of our 2016 earnings to shareholders through common dividends and share repurchases. At the same time, our capital ratios remain robust. Under Basel III, the Tier 1 ratio was estimated at 11.9% and the Common Equity Tier 1 ratio was estimated at 11.1%. On a fully phased-in basis, Common Equity Tier 1 was estimated at 11%, and we were also fully compliant with a liquidity coverage ratio rule at the end of the year and our liquidity position remained solid with a historically low loan-to-deposit ratio of 81%.

So as we look ahead in terms of 2017, the targets that we laid out are as follows. We expect full year average loans and average deposits to grow in the low single digits. Our expectation for net interest income and other financing income growth is in the 2% to 4% range, and our adjusted non-interest income is expected to grow 3% to 5%.

From an expense standpoint, total adjusted non-interest expenses in 2017 are expected to increase between zero and 1%, and we expect to achieve a full-year adjusted efficiency ratio of approximately 62%, with positive adjusted operating leverage in the 2% to 4% range. From a credit standpoint, full-year net charge-offs are expected to be 35 to 50 basis points.

So in closing, our solid 2016 results reflect the successful execution of our strategic plan and our commitment to our three primary strategic initiatives, which are growing and diversifying our revenue streams, practicing disciplined expense management, and effectively deploying our capital. We're pleased to end the year on a positive note and believe we have the right team and the right strategy to deliver and create further shareholder value in 2017.

And with that, we thank you for your time and attention this morning. And I'll turn the call back over to Dana for instructions on the Q&A portion of the call.

Dana W. Nolan

Executive Vice President - Head of Investor Relations, Regions Financial Corp.

Thank you, David. Before we begin the Q&A, as a courtesy to others, please limit your questions to one primary question and one follow-up. We will now open the line for questions.

QUESTION AND ANSWER SECTION

Operator: The floor is now open for your questions. [Operator Instructions] Your first question comes from Matt Burnell of Wells Fargo.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

Good morning, Matt.

Matthew Hart Burnell
Analyst, Wells Fargo Securities LLC

Q

Good morning, Grayson. Thanks for taking my question. You mentioned a couple of times the momentum in the Commercial side of the business, and I want to focus a little bit on the small and medium-sized borrowers. And obviously, the competition there has been very, very intense. But do you sense a greater level of optimism from your customers that might increase their desire to borrow over the next year or two, presuming we get a little bit of benefit in the economy? And then I have a bigger picture question for my follow-up.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

Absolutely. I'll only make a few comments, and then I'll ask John Turner, who manages that part of the business for us, to make his comments as well. Absolutely, we're seeing anecdotally in our conversations with our customers a lot more confidence and a lot more optimism about what the future will hold. And we continue to believe that, at some point that turns into more business activity than we've seen thus far.

But that being said, we're still not seeing that enthusiasm turn into actual lending activity. Line utilization is still not showing signs of that enthusiasm turning into activity, nor are we seeing applications of credits do that. But having said that, I can't underscore enough the amount of optimism we hear in the voices of our customers. But I think it's going to take some time yet for that to result in a lot of economic activity.

John, if you would?

John Turner
Senior Executive Vice President-Head of Corporate Banking Group, Regions Financial Corp.

A

Yeah. Thanks, Grayson. I just would add and reiterate, we are hearing more positive outlook for our customers, but we're not seeing that translate into new opportunities yet. Pipelines are up a little. Line utilization is down about 90 basis points in the quarter. We're having meaningful conversations with customers, but none of that has yet resulted in their desire to increase business fixed investment, which ultimately is what we need to see growth.

Matthew Hart Burnell
Analyst, Wells Fargo Securities LLC

Q

Okay. Thanks.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

Matt, do you have a follow-up question?

Matthew Hart Burnell
Analyst, Wells Fargo Securities LLC

Q

Yeah. My question really relates to the deposit rates, which actually went down a little bit quarter-over-quarter, which was a little bit better than we've seen at some of your competitors. Do you attribute that to just the location of your franchise, or is there something else going on there? And then maybe an update on your thinking of deposit beta as rates rise and where you are now relative to sort of your longer-term assumption.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

Well, I think, Matt, when you look at our franchise, I mean, the real competitive advantage we have is really as a deposit gathering franchise, that's where the real value of our bank is at. And you look at our deposit portfolio, it's a very granular portfolio and about 50% of that portfolio is located in smaller community markets. And if you look at our thoughts and our forecast, you see a very conservative beta forecast for interest rate increases.

Candidly, the environment we're coming from right now, we've never seen before. So, this is new coming from this interest rate environment to start to increase. We're optimistic that our deposit betas will provide an advantage for us. And thus far, as you mentioned, our deposit cost has remained relatively low. I think we're up 1 basis point quarter-over-quarter. So, we think we've done a very good job actually growing deposits in the face of that activity.

David, you may want to add to that.

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

A

Yeah, it's a great question, Matt, because, as Grayson mentioned, this is really our competitive advantage that we've been waiting to see come through in our income statement. As Grayson mentioned, the deposit makeup that we have really resulted in last cycle, we had one of the lower betas than any of the peers. I think we were internally at about 54% was our beta. Perhaps it will be higher because we're at historical lows, and so we model a 60% beta as the terminal value, but we start slow in that 40% range and we think that's really going to be important.

Deposit rates, we think, the faster rates increase from the Fed, the more pressure there will be. But what's happened thus far is we haven't had, nor have many in the industry had to pass much through to deposit holders, because we've had increases one-off. So we're looking forward to dealing with that. We have great liquidity and a great stable funding base that we think can create value for shareholders in 2017 and beyond.

Matthew Hart Burnell
Analyst, Wells Fargo Securities LLC

Q

Thanks very much.

Operator: Your next question comes from Michael Rose of Raymond James.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

Good morning, Mike.

Michael Rose
Analyst, Raymond James & Associates, Inc.
Q

Hey, good morning. Maybe just a question for David on the margins. Sorry if I missed this, but can you quantify the impact of premium amortization on the margin this quarter? And then maybe just some greater context as to what your forecast includes for NII. Does it include a couple of rate hikes, I assume, and what would it look like if we didn't get any rate hikes? Thanks.

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

Yeah. So you saw our change in premium amortization early on. It was about 1 point difference on that in terms of margin. Clearly, the increase in rates was the big driver for us, and that is not just a Fed move, but really LIBOR starting to move in advance of that, as well as the tenure. So that's very helpful to us, as we continue to be – and our sensitivity continues to be on the longer end. Today between – the short end is probably 42% of our sensitivity and 58% in the middle for the back end.

So as we think about increases in – for this next year, we're closer to where the market is right now, which was having a rate increase sometime in the summer and maybe one towards the back end of the year. Now we realized what [ph] Jerry Allen (32:14) said the other day with regards to supporting the dot plots, and perhaps there's an incremental increase baked into that, but we don't forecast that. If we get it, then that's better for us, but our guidance that we just laid out really shows that increase in sometime in the summer, and then towards the back end of the fourth quarter.

Michael Rose
Analyst, Raymond James & Associates, Inc.
Q

Okay. That's helpful. Maybe as my follow-up, if you can just give some color on some of the major fee income businesses. Given the guide, I know capital markets was down, I guess, greater than I expected sequentially, and maybe if you can just give the outlook for some of the businesses for this year. Thanks.

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

Yeah, I think – so we have a good story for non-interest income. Clearly, there's a lot of seasonality that hits that space. You can see that manifest throughout the industry. Same thing for us, in particular we came off a lot of really strong third quarter in a number of areas, capital markets and wealth management. We believe those rebound, and that's why we have our guidance for non-interest revenue growth of 3% to 5% next year. We went into this year with a 4% to 6% expectation. We ended up growing 7%. So, we feel confident about our ability to grow in that 3% to 5% range. It will be a contribution for all those line items that you've seen in the past, as we continue to just grow customers and continue to build out certain of our new platforms, like BlackArch Partners.

Michael Rose
Analyst, Raymond James & Associates, Inc.
Q

That's great color. Thanks for taking my questions.

Operator: Your next question comes from Betsy Graseck of Morgan Stanley.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp. A

Good morning, Betsy.

Elizabeth Lynn Graseck
Analyst, Morgan Stanley & Co. LLC Q

Hi. How are you?

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp. A

[ph] I'm well (34:07).

Elizabeth Lynn Graseck
Analyst, Morgan Stanley & Co. LLC Q

Great. I had a couple of questions. One was on the performance around the capital market investments that you're doing and the treasury management investments. I was wondering how you think those are going to come through as you go through 2017.

John Turner
Senior Executive Vice President-Head of Corporate Banking Group, Regions Financial Corp. A

Betsy, this is John Turner. I would say we're very pleased with the investments we've made. Capital markets revenue was up 44% last year in 2016. We did see, obviously, some decline in the fourth quarter, but that business is going to be uneven. The M&A advisory fee income that we enjoyed was more front-end loaded into the second and third quarter.

And so, as we look forward to 2017, we face some headwinds in a few of our newer initiatives, like the Low Income Housing Tax Credit platform that we acquired, CMBS platform that we've established. The conditions in the market aren't great for those today, but we think they will ultimately work themselves out. We feel very good about the initiatives and the investments, and expect to continue to grow capital markets revenue and treasury management revenue in 2017 at a pretty good pace.

Elizabeth Lynn Graseck
Analyst, Morgan Stanley & Co. LLC Q

I mean, a rising rate environment should be good for treasury management, I would expect.

John Turner
Senior Executive Vice President-Head of Corporate Banking Group, Regions Financial Corp. A

It will be, and remember that, if you look at our deposit growth, we grew deposits by over $1.2 billion in the Corporate Bank, and that's really a reflection of our focus on relationships, building broader and deeper relationships with our customers, and winning more treasury management business than we have in the past. And so I think you will continue to see that grow.

Elizabeth Lynn Graseck
Analyst, Morgan Stanley & Co. LLC Q

Okay. Thanks. And then just second question on the cost save initiatives that you've been very clear about the targets. Could you give us a sense as to how the efficiency will drop to bottom line? As you go through the year, is there any kind of trajectory that we should expect? Is there back-end loaded or what?

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

I think you look at rates, if the rate curve will hold, you'll start seeing even a better improvement as we get towards the end of the year. We should start out having a pretty decent efficiency ratio contribution to that 62% that I had talked to you about. But it gets even better as we get to the back end of the year.

Elizabeth Lynn Graseck
Analyst, Morgan Stanley & Co. LLC
Q

Okay. All right. Thank you.

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

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.
A

Good morning, John.

John Pancari
Analyst, Evercore ISI
Q

Good morning. Grayson, if you could just talk a little bit about the fact that you've gotten a satisfactory rating on the CRA, as you mentioned, what are your – does that pave the way for you to consider acquisitions again? And if so, can you give us your updated appetite for whole bank deals and then non-bank deals? Thanks.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.
A

Yeah. I mean, John, I think that, first of all, we are very pleased to get our CRA rating reinstated back to satisfactory. The team here worked very hard to accommodate that. And so it's indicative the way we do business and the way we try to help our customers in all of the communities we operate in. So, very encouraged by that turn of events.

What does that mean for us? We're very focused on organic growth. We're very focused on optimizing our distribution channels. You saw in 2016 that we invested in all of our channels, our online banking, our mobile banking, our contact centers, our ATMs, and our branches. We had a number of consolidations in the 2016 and opened relatively few branches in 2016. You can see that – but at the same time, we invested a tremendous amount on technology into those branches and changed our delivery format in a number of those offices to be more efficient and more effective.

You'll see us continue to do that. We think that it's an important and critical part of our franchise value, and we think all of our distribution channels are important. The branch still has an awful lot of relevance, and it's still the predominant channel that customer choose to open new accounts with us. So our primary focus is organic growth.

When it comes to acquisition opportunities, we're very sensitive to what's going on in the market. We have a team inside the bank that spends an awful lot of time monitoring markets and what's going on there. We look for opportunities to invest through acquisition. You saw last year that that was predominantly done through non-bank bolt-on acquisitions, which has been predominantly our interest.

We look at whole bank deals. Quite candidly, where valuations are at right now, I think some of the economics of that, we find challenging. But there may be opportunities for that. We're watching, but our primary focus is on growing organically. So we'll watch and see where the market goes. But at this particular point in time, we see most of our opportunity in growing organically, in growing in non-bank bolt-on acquisitions, and we're monitoring whole bank acquisition opportunities. But right now, that market seems to be improving. I think it's early yet. It's early yet.

John Pancari
Analyst, Evercore ISI

Q

Okay. All right. Thanks. And then separately, I know you've mentioned that you're focusing increasingly on risk-adjusted returns and that, to a degree, has impacted your loan growth in the quarter and possibly your outlook. So, I guess, if you could just talk a little bit more about identifying these exact areas or exact portfolios where you're deliberately de-emphasizing production as you're focusing on the risk-adjusted returns. Thanks.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

Well, I mean, the – first of all, we recognize we're in a cyclical business, and we have to be mindful of that as we establish our risk appetite across different lending segments. And we spend an awful lot of time trying to adjust our risk appetite, is based on where we think we are in the cycle with those different lending categories.

We've signaled to you that we've throttled back on indirect auto. We've throttled back on investor real estate construction. We've throttled back on multi-family, to a certain degree. But we're still in those businesses, still lending in those businesses. And, obviously, the one business that we've been most cautious in is energy, for apparent reasons. But we still are in all of these businesses. We're just being more thoughtful, more careful, given where we're at in the cycle of that.

But we also spend an awful lot of time on both business that we win and business that we lose. We compete in a lot of different markets against very large financial institutions and small community banks as well. And there's an awful lot of competition there and we're trying to be very thoughtful about what type of transactions we'll do, what kind of risk-adjusted return we can achieve in those. And I think in this market we're able to grow our business in asset classes that we think make a lot of sense.

As David said, we believe, for 2017 we'll grow in the low-single digits, but that is growing faster than that in some segments, while constraining growth in some of the other segments. I think most of this discussion centers around some of our commercial lending activities, so I'll ask John Turner to make a few comments as well.

John Turner
Senior Executive Vice President-Head of Corporate Banking Group, Regions Financial Corp.

A

John, I think we've talked about, as an example, our focus on risk-adjusted returns in our shared national credit book and we spent a lot of time there this year as a result of what we refer to as recycling activity, where we've exited some relationships and entered new ones. We've seen the level of credit-only shared national credits come down by about 16%.

The revenue that we're generating per relationship in those newer relationships go up by 35%. They generate over 100% more non-interest revenue, and the risk-adjusted returns are 220 basis points greater than those relationships that we exited.

In addition to that, I talked about deposit growth. We saw fee income growth in the business. And the overall risk-adjusted return on the Corporate Banking business here at Regions, inclusive of all three businesses, is up 160 basis points year-over-year.

And at the same time, we think we have a better quality loan portfolio as we're de-risking the business and adding better risk and getting an appropriate return. We think that our commitment to profitable growth and appropriate returns is paying off and we'll continue to see that in the coming quarters.

John Pancari
Analyst, Evercore ISI

Q

Got it. All right. Thank you.

Operator: Your next question comes from John McDonald of Bernstein.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

John, good morning.

John Eamon McDonald
Analyst, Sanford C. Bernstein & Co. LLC

Q

Hi. Good morning, guys. David, I wanted to follow-up on the net interest income margin question. Is there a rule of thumb that we can use in terms of, as we try to model Fed hikes for you guys, how much each Fed hike of 25 basis points adds to net interest margin, any rough rule of thumb there?

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

A

Well, we've tried to give you the parallel shift of 100 basis points. It's about $160 million right now, and then we're 42% on the short end of that. If you do some quick math, depending on what beta assumption you want to use, you're talking about $15 million, maybe $20 million on an annual basis. And again, the beta assumption makes a difference.

John Eamon McDonald
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay. That's helpful. And then just following up on the efficiency, the target this year, the 62%, at a conference in December you guys laid out a longer term, kind of sub-60%, and I think you said by 2018. Is that the right way to think about it that you could go from 62% to 60% by the end of 2018? Does that imply a real ramp-up in the expense saves next year?

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

A

Well, so we can get to the 60s, that's our commitment, by the end of 2018 kind of on a run rate basis there. So, you'll see us continuing to chip away at it each and every quarter through 2018 so that by the time we get there, we're hitting the 60% and below target that we laid out. And then, by the time we get there, we'll reassess and give you our new target because over time we think we'll be even south of that. But we're – let's get to the below 60% first, the [ph] one we established (45:42).

John Eamon McDonald
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay. [ph] Fair enough (45:45).

Operator: We'll proceed to the next question, which comes from Geoffrey Elliott of Autonomous Research.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

Hi, Geoffrey.

Geoffrey Elliott
Analyst, Autonomous Research LLP

Q

Good morning. Thank you for taking the question. It looks like there was quite a bit of strength in service charges this quarter. I wondered if you could elaborate on what happened there.

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

A

Yeah. I'm not sure what you're looking at from a stress standpoint. Service charge is continuing to be fairly strong for us.

Geoffrey Elliott
Analyst, Autonomous Research LLP

Q

I said strength. I said strength, not stress.

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

A

Oh, I'm sorry. We heard stress. Okay.

Geoffrey Elliott
Analyst, Autonomous Research LLP

Q

Maybe it's the British accent or something.

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

A

Sorry. We're truly strong. We have such a strong retail network, continuing to grow customers is important and you're seeing that manifest itself in service charges. We've also had increases in customers on the Commercial side as well. So, if you look year-over-year, we're kind of flat. We were overcoming some obstacles last year on posting order. And we expect service charge continue to be robust in 2017.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.
A

No, I mean, we've done a really good job in our Consumer Bank. And if you look at growth metrics across accounts and account activity and the quality of the accounts we're placing on our books, we continue to be encouraged by the progress we're making. And if we do that, it really improves a number of revenue streams.

Geoffrey Elliott
Analyst, Autonomous Research LLP
Q

And if the economy strengthens, how does that impact this? Do people make less use of overdraft if they're feeling better off or the dynamic is kind of more complex?

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

From my perspective, there are certain people [ph] less would (47:53) happens and these aren't all overdrafts, by the way. These are core service charges, so that are monthly maintenance fees and those things. So stronger economy we don't think would do anything, but help that. And it's really the customer growth that we continue to have that we think is most impactful to that line item and the more robust economy with the outreach that we want to do to continue to expand the franchise and grow relationships, we think that could be a positive for us in 2017.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.
A

Yeah. And what we've seen – when you look at the consumer base, we've really – have started, really, shift in the mix of fee income and our consumer book towards more around activity-based, in particular on debit cards and credit cards, less reliance on overdraft activity. And as you look at our checking account features, we've introduced a number of new products that give customers more assurance, more safety that they transact business in the correct way. And so, we feel real good about our offerings, we feel good about our growth, and we think 2017 you'll continue to see this sort of pace of momentum that we have really started generating in 2016.

Geoffrey Elliott
Analyst, Autonomous Research LLP
Q

Thank you.

Operator: Your next question comes from Ken Usdin of Jefferies.

Kenneth M. Usdin
Analyst, Jefferies LLC
Q

Hi. Thanks. Good morning.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.
A

Good morning.

Kenneth M. Usdin
Analyst, Jefferies LLC
Q

Dave, I was wondering if you could talk a little bit about just total balance sheet size. I think we understand the expectation for loan and deposit growth. You guys have been at a pretty comfortable level of securities, and it sounded like you did a little bit more remixing. So is it fair to say that you're comfortable with kind of at this level of earning assets or what would drive the total size of the balance sheet from here, unless you started to just take on some wholesale funding?

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

A

Yeah. It's great question, Ken. Part of what we did this year is we were looking at our – certain of our deposit products. We talked about the collateralized deposits that were in our Wealth Management group. Those didn't – weren't providing virtually any liquidity value for us, and certain of those were more expensive. So, we decided that we would move those out of the bank. And so if you look at deposit balances, you really need to go to the supplemental page 22 and see what the makeup is, because we had good deposit growth in Consumer and in business services – or the Corporate Bank segment.

As we think about next year, low single digit growth relative to loans and deposits, we think earning assets can grow in that 2% range. And we know that didn't happen this year, but we think that that can happen as we go through 2017.

Kenneth M. Usdin
Analyst, Jefferies LLC

Q

Okay, got it. And would that increment be then – you did issue a bunch more debt in the fourth quarter. Would that be also funded by more debt issuance this year?

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

A

Those are really FHLB advances, and we're expecting our continued deposit growth to fund our activities on the left side of the balance sheet.

Kenneth M. Usdin
Analyst, Jefferies LLC

Q

Okay. And just one follow-up on the securities portfolio. Outside of the premium amortization help to secure these deals, I'm just wondering at what point – how close are you to kind of getting to that back book, front book in terms of just new yields on new purchases versus what's rolling off the book.

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

A

Yeah. So we've talked about where things settle down a little bit on premium amortization being closer to that treasury yield of 2.75% and that we would settle on premium amortization – premium amortization, we settle in that mid-$30 million range. But going on today, it's about 2.50% in terms of the mortgage-backed. Corporates are about 1 point higher than that. And so we continue to see further benefit from rising rates on that portfolio, primarily through the slowing down of premium amortization.

Kenneth M. Usdin
Analyst, Jefferies LLC

Q

Okay.

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

So the new securities that we're putting on are accretive to our costs.

Kenneth M. Usdin
Analyst, Jefferies LLC Q

Right. Outside of the premium benefit, they're now accretive to the underlying?

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

That's right.

Kenneth M. Usdin
Analyst, Jefferies LLC Q

Okay. Got it. All right. Thanks a lot.

Operator: Your next question comes from Matt O'Connor of Deutsche Bank.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp. A

Good morning, Matt.

Robert F. Placet
Analyst, Deutsche Bank Securities, Inc. Q

Hey, guys. This is Rob from Matt's team. Just had a follow-up on your outlook for commercial loan growth. I was just curious, how much additional balance reductions we should expect in those specific Commercial segments, such as energy and multi-family, or are you guys just about done at this point in terms of balance reductions there?

John Turner
Senior Executive Vice President-Head of Corporate Banking Group, Regions Financial Corp. A

Yeah. John Turner. Yeah, I would say that we expect the runoff at energy to begin to moderate. We'll certainly have some continued pay-downs as some of the problem credits work themselves out, but there's good stability in that marketplace. We're seeing asset sales occur. We're seeing opportunities, though limited thus far, to potentially lend into the space. And we did actually make two new E&P loans in 2016; one towards the end of the year. So I think we'll see runoff moderate.

With respect to multi-family, remember, we are trying to change our mix of business from being primarily construction-oriented to a better mix of construction and term. And we can't match the timing. And so what we've seen is runoff in the construction book as our term lending initiative is getting some traction. And so we've had more runoff in that portfolio than we anticipated.

At some point, we bottom out and begin to grow as the term loan initiative picks up. And, again, we are projecting 2% to 4% loan growth in 2017. We think that will come in some measure from our specialized lending groups, where we can lean into the expertise that we have in technology, defense and healthcare, in power utilities, as an example, and also within our Regions Business Capital group, where we think we have an awfully good level of expertise and opportunity to grow our business.

Robert F. Placet
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. Thanks. And just separately, on the net interest margin, any color on where you see the consolidated NIM coming in for 1Q? I know you have some benefit from premium am., but any other puts and takes? Will you see additional benefit from the December rate hike this quarter as well?

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

A

Yeah. This is David. From a NIM standpoint, we still will get the benefit of lower rates now for the full quarter, which we think will be meaningful, and we'll pick up a couple of points with lower premium amortization as well. But don't dismiss the impact of two less days in the quarter, which actually is accretive to the NIM, and that'll be 2, 3 points in and of itself. So as you think about where we might be in the first quarter, we could be up in that low to 3.20% – in the low-3.20s then and continuing to improve – if the rate environment will hold, continuing to improve from there towards the fourth quarter.

Robert F. Placet
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. Thanks.

Operator: Your next question comes from Steve Moss of FBR.

Steve Moss
Analyst, FBR Capital Markets & Co.

Q

Good morning. I was wondering on capital deployment here. Could you just give us a little more color as to what you're thinking about how aggressive you could be for your 2017 CCAR ask?

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

A

So we go through a very deliberate, thoughtful process on capital deployment. You saw that this past year, where we returned $1.2 billion to our shareholders, which was more than our earnings at the end of the day. We will continue to – it's important for us to get our capital optimized. One of our key metrics that we talk about is getting to that 12% to 14% return on tangible common equity in 2018.

And to do that, we have to have an optimal size of capital for the risk attendant in our balance sheet. And so clearly, we've had a challenge of that capital base being as strong as it is with where were loans this past year. So, we'll be evaluating that for our submission. And I think we learned a few things through other submissions this past year on others that had a capital return in excess of 100% of earnings, and I think that we will make a prudent decision.

Again, our primary focus is to ensure, first and foremost, that we have the right amount of capital to run the company. And then that excess capital, we need to use it up appropriately. Grayson talked about organic growth, bolt-on acquisitions, and when those don't use up your capital base, returning it to the shareholders is the right thing to do, and we will continue to do that through our planning.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

But, again, I'll just reiterate that our primary desire is to be able to use the capital we generate to grow our business and serve our customers organically. And as we use our team internally to put together our capital plan this year for approval by our board, a lot of what we decide to do will be based on our outlook that we have for potential organic growth. And if we – depending on our outlook, it will drive really what we do to deploy capital otherwise.

Steve Moss
Analyst, FBR Capital Markets & Co.

Q

Okay. And then my follow-up question with regard to your loan loss reserve ratio, it's been coming down last couple of quarters. Kind of wondering where you think it could [ph] tail out (58:36) by year-end.

Barbara I. Godin
Chief Credit Officer & Senior Executive Vice President, Regions Financial Corp.

A

This is Barb Godin. Again, as you know, we go through a very thoughtful process on setting the reserve for loan losses. As we continue to see the energy portfolio improve, I would say, you will also continue to see some improvement in that level of reserve. I'll reiterate what I've said in the past. I never see it going back down to that 1% level. At some point, it will probably bottom out somewhere in that 1.25% or so.

Steve Moss
Analyst, FBR Capital Markets & Co.

Q

Great. Thank you very much.

Operator: Your next question comes from Saul Martinez of UBS.

Saul Martinez
Analyst, UBS Securities LLC

Q

Hi. Good morning. Thanks for taking my question. I wanted to ask about your branch rationalization strategy, especially in the context of what is your competitive strength, your low cost funding. It's a pretty sizeable reduction and your branch footprint is probably more geared on average in lesser competitive markets that, obviously, gives you a very strong low cost funding.

But when you think about your branch rationalization strategy where you cut, how do you think about that? What are some of the variables you look at and how do you ensure you're not cutting into your strengths? And I guess as an adjunct to that, how should we think about the economic benefits you get from the branch closures? The 150 branches or so, is there a way to systematically think about how that flows through to your bottom line?

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

Well, first of all, that's a very thoughtful, data-driven process, because we're looking at all of our markets, how each branch is performing, whether transaction activity in that branch is growing or declining. You hear a lot of institutions talk about average growth rates, average decline rates in transactions. Those averages can be very deceptive, because we have branches where transactions continue to grow year-after-year. But what we've done is to try to take a very facts-based, data-driven process to determine where we have opportunities to not only consolidate offices, but to serve our customers even better. And so, we look very closely at proximity of our branch offices to where our customers live and work. We spend an awful lot of time making sure that we do this the right way.

We believe the branches are still very relevant. We still believe that there's opportunities to rationalize that particular distribution channel. But we have to be careful how it fits in with all of our other channels and make sure that at the end of the day, we're still able to attract and retain and service customers with excellence. So, John, all of these branches report to you. If you would sort of speak to that.

John Turner

Senior Executive Vice President-Head of Corporate Banking Group, Regions Financial Corp.

A

Sure, Grayson. Just kind of level set a few – kind of step back for a minute. We peaked about 10 years ago in 2007 with 2,127 branches. We're down 600 branches. We're down 28%, which is really more than anybody else in the industry. A couple of drivers there, you talk about proximity and things like that. That is a big part of it.

The other part of it is, we've made a lot of investments in mobile and online banking and really driving those transactions out of the branches that are what I'd call service transactions. So, check your balance, make a deposit, move money around, pay bills. So a lot of those things have been moved really out of the branches and moved to the mobile and online banking platform.

The other comment I would make is, we've done a lot of work around what we call Universal Banker. And Universal Banker really has helped us from productivity standpoint by allowing us to have staffing at reduced levels in our branches. I would tell you, for 2016, between our 103 branch consolidation and our Universal Banker strategy, we reduced about 800 positions just resulting from those two items, so it really is a balance.

So we take balanced approach around what we're doing in mobile and online, what we're doing with our deposits for an ATM strategy, what we're doing with our virtual and terminal strategy, and also consolidations. I will tell you, over the next probably year or two, you will see consolidations outpace any building. So our net branch count will go down from the 1,527 level today, will probably be in that, I'd say, 1,480 to 1,500 range. But again, branches are very important as part of our strategy.

David J. Turner, Jr.

Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.

A

This is David. I'll add one thing for your last part of your question is that when we look at this from an economic standpoint, we consolidate a branch, we're going to lose some revenue. So the goal is to take out more costs than any revenue that you might lose. And for us, we target about a two-year payback. And when we consolidate these branches, thus far the wave that we've had, the 103 this year, the ones last year, been slightly less than a two-year payback. So, we feel very good about how they're paying for themselves, and it's a part of our expense initiative as well.

John Turner

Senior Executive Vice President-Head of Corporate Banking Group, Regions Financial Corp.

A

The other point I would make, even though we have less branches, our account growth is up. We're growing our account base in checking account in that 1.7%, 2% range. And now banking growth is up in that 13% to 14% range. Credit card growth is over 10%, 11% range. So we're seeing strong growth in spite of the fact we have less physical stores. Our revenue per branch is up also.

Saul Martinez
Analyst, UBS Securities LLC

Q

Okay. No, that's helpful. Thank you for that. And if I could just follow-up on loan growth, and you're assuming in your 2017 guidance 2%, 2.5% real GDP growth. How do you think about the potential upside of that number, maybe not in 2017, but looking out late 2017 into 2018?

If we do get a bit better economic growth environment, I assume it's not a linear relationship. Risk appetite might move up, [ph] animal spirits (01:04:50) and whatnot, but how do you think about the potential upside if the environment really does improve?

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

Well, I mean, it's hard to put a number around, but it's – we're optimistic that as we look forward that there may be considerable upside to our forecast. What we're trying to do is to balance our emotions between what we know is going on today, what we know we can deliver, and what we hope the future may hold for us. There's an awful lot of enthusiasm, a lot of people that are appearing to get more courage to invest, more courage to expand. But we still are trying to balance that in our markets. It's a great turn of emotions in our marketplace. We really are excited about what the potential upside might be.

That being said, at the end of the day, from a forecast standpoint, we've still got to forecast what we know we can deliver. And so we're trying to balance that, as I'm sure you are. I'm not sure there's a solid answer to your question, but I do believe that there is a potential for considerable upside.

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

A

I think to your point, though, in terms of 2017 is probably a lot of this has to manifest itself in 2017 for the effect to take in 2018 and 2019. So, I think we have a lot to learn here with over the incoming months to see what the administration really does.

John Turner
Senior Executive Vice President-Head of Corporate Banking Group, Regions Financial Corp.

A

The only thing I'll add, if you think about our business, the commercial and middle market, small business customer represents about 25%, give or take, of the base profitability. And that customer has not been borrowing for years. And so if we begin to see a little extra pickup in the economy, particularly amongst the middle market customer base, small business customer, I think there's a lot of upside...

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

[indiscernible] (01:06:50).

John Turner
Senior Executive Vice President-Head of Corporate Banking Group, Regions Financial Corp.

A

...for our company, absolutely.

Saul Martinez
Analyst, UBS Securities LLC

Q

That's good color. Thanks a lot.

Operator: We have time for one more question. Your final question comes from Gerard Cassidy of RBC Capital Markets.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

Hey, Gerard.

Gerard Cassidy
Analyst, RBC Capital Markets LLC

Q

Good afternoon, guys. Thank you. David, can we go back to the capital question? You talked about, with this year's CCAR, that you're always going to want to keep the right amount of capital to run your business, and I think in the past you may have used the 9% number. Is that still an appropriate number for the risk on the balance sheet?

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

A

Yeah, it's a good question, Gerard. We use a 9.5% Common Equity Tier 1 and it's kind of the range that we think we ought to have based on today's risk. We're, obviously, looking at different portfolios and we've de-risked a little bit. As we do that, that number can go down. We also have added portfolios that have more risk to them. That goes the other way, but right now we think 9.5% is probably a good target.

Gerard Cassidy
Analyst, RBC Capital Markets LLC

Q

Good. And then, you, I think, also referenced in talking about this that you're looking at what other banks have done in terms of the ask in CCAR possibly going over 100% of earnings. With the proposed change for the under $250 billion in asset banks not having to go through the qualitative portion of the exam, does that give you more confidence to ask for a bigger number in view of what some of the banks did last year, but now it has changed as well?

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

A

Well, certainly, the removal of a qualitative aspect of this CCAR is incrementally helpful, but it's not a free pass. The regulatory supervisors are still engaged very closely with our capital planning and governance processes. It just happens in a different time of the year. It'll most likely happen in the third, fourth quarters as we prepare for an April delivery each year. And this year is a transition year, so it will take some time. But not having the qualitative aspects and being able to leverage the models that we've built that have been reviewed over a number of years is where we get our confidence. We need to run our bank with the idea of what capital we think and our board thinks we need to have.

We know we're regulated, and we have to evaluate that, too. But the regulators aren't looking for us to try to outguess them. They're trying to get us to run our bank appropriately, and that's why we feel confident about being able to get our capital down to that 9.5% Common Equity Tier 1 over time in a prudent manner.

And so, we're going to march in that direction. The pace of which is going to be determined through further analysis. But that is really important for us to get to that 9.5%, as we set our goal on return on tangible common of 12% to 14%, which embedded in that is getting our capital optimized and right-sized.

O. B. Grayson Hall

Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

But the capital planning process has made constructive progress every year. And we look at how the process has changed from last year to this year. And we think it's been very constructive, gives us more certainty, it gives us more confidence. And I think that we have really developed a very rigorous, very disciplined capital planning process inside our company. And we got a lot of confidence that we can do the appropriate things given the risk in our balance sheet. And so, we continue to build confidence around our ability to manage [ph] cap (01:10:27).

Gerard Cassidy

Analyst, RBC Capital Markets LLC

Q

Very good. And then, just as a follow-up, you guys have done a very good job in closing down branches and, in your answers today, some good analysis of how you look at it. Have you taken into account for this – the upcoming year and the branch closures that in a rising rate environment, deposit behavior may be different and [ph] would that a (01:10:50) sector modeling on your payback? I think, David, you mentioned that's two years or less than two years. Have you factored that into the equation yet?

David J. Turner, Jr.

Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.

A

Well, a couple of things on that. Yeah, we have and we try to anticipate deposit behavior. A couple of things that are happening. One, we have a loan deposit ratio of 81%, so we're in pretty good position there from a liquidity standpoint. Relationship bank has mattered and will matter going forward. We also recognize that TLAC for the larger players have caused them to have a different liquidity profile than they otherwise would have had, and therefore, perhaps the competition regarding deposits, especially in a 1% – low-single digit, 2%, 3% loan growth mode then put as much pressure on deposits and deposit rates.

The growing – making investments that we want to – John talked about the retail network strategy of getting in the – some of the major metros and being able to be in places where you'll grow deposits is really important to us in 2017 and beyond.

O. B. Grayson Hall

Chairman, President & Chief Executive Officer, Regions Financial Corp.

A

But if you look at 2016 and even prior to that, we've been in – yeah, our strategy has been to re-mix our deposit portfolio to make it more granular, to make it less interest rate sensitive. And most of our growth has come in low-cost deposits and we've also reduced our dependency on higher-cost deposits and also our dependency on deposits that require collateralization.

When you look at where we're at today, we've ran some limited exercises to try to better understand how much we would have to move rates to attract new deposits into the company. And we think we have a pretty good handle on how customers will react in higher markets in a higher rate environment and continue to be hopeful that our deposit betas will outperform.

David J. Turner, Jr.

Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.

A

Gerard, I'll add one other thing. If you look at our supplement, on page 22, you'll see our deposits broken out by consumer, corporate, wealth management. You'll see our wealth management year-over-year was down $2.2 billion, and that's a decision we made that we weren't getting the kind of liquidity that we wanted. If we needed to, we could change our tune on that and we might have to pay up a little bit for deposit. But we have multiple avenues of funding. And our liquidity position, in particular related to our securities portfolio and other assets that we can post up as collateral for the FHLB is very strong which, I think, will bode well for us not having to chase these deposits or be unduly restrictive on our consolidation efforts.

Gerard Cassidy
Analyst, RBC Capital Markets LLC

Q

Great. Thank you for the thorough answer. I appreciate it.

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

A

All right.

O. B. Grayson Hall
Chairman, President & Chief Executive Officer, Regions Financial Corp.

Thank you. That was our last question. We appreciate everyone's attendance today and we'll stand adjourned. Thank you.

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

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