WSFS FINANCIAL CORPORATION

Moderator: Steve Fowle
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1:00 p.m. ET

Operator: Good day, ladies and gentlemen, and welcome to the WSFS Financial Corporation first-quarter 2014 earnings conference call.

All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question and answer session. If you would like to ask a question during this time, simply press star then the number one on your telephone keypad. If you would like to withdraw your question, press the pound key.

As a reminder, this call is being recorded. I would now like to introduce your host for today's conference, Steve Fowle, Chief Financial Officer. Please go ahead, sir.

Steve Fowle: Thank you, Danielle, and thanks to all of you for taking the time to participate on this call. With me from WSFS are Mark Turner, President and CEO; Paul Geraghty, our Chief Wealth Officer; Rodger Levenson, our Chief Commercial Banking Officer; and Rick Wright, our Chief Retail Banking Officer. Before Mark begins with his opening remarks, I'd like to read our Safe Harbor statement.

Our discussion today will include information about our Management's view of our future expectations, plans, and prospects that constitute forward-looking statements. Actual results may differ materially from historical results or those indicated by these forward-looking statements due to risks and uncertainties, including but not limited to, the risk factors included in our annual report on Form 10-K, and our most recent quarterly reports on Form 10-Q, as well as other documents we will periodically file with the Securities and Exchange Commission. With that said, I'll turn the call over to Mark Turner.

Mark Turner: Thanks, Steve. And thanks to everyone on the call for your time and attention.

WSFS reported $16.9 million in net income and $1.85 per share in earnings in the first quarter. Excluding notable items identified in the release, the largest of which was a $6.7 million, or $0.73 per share, tax benefit from the legal call of our reverse mortgage trust, more normal earnings were $1.10 per share in the quarter.

As indicated in last quarter's call and this quarter's release, the first quarter is by far our most seasonally slow quarter, and this year that was exacerbated by the long and harsh winter in the Mid-Atlantic States.

Despite those dynamics, we continued the fundamental growth and momentum of our Business.

Highlights include: core total revenues, net interest income, and core fee income (that is, excluding securities gains) all increased a healthy 8 percent from the same quarter 2013, with that strength coming from every major business line.

Continuing that momentum, this quarter's total loans grew by 5 percent annualized, propelled by commercial loans, our most profitable loan segment, which grew 9 percent on an annualized basis.

And core customer funding, excluding the expected runoff in temporary trust account activity, increased 5 percent on an annualized basis in the quarter. Core funding now represents a robust 84 percent of our total customer funding.

Our core earnings per share of $1.10 (again, that's excluding the notable items) was 22 percent greater than same quarter last year, and our core Return On Assets of 90 basis points, was 9 basis points, or 11 percent, greater than the same quarter last year, as well.

Lastly, tangible common equity and tangible common book value per share both increased more than 7 percent in this quarter alone, coming from net income and an improvement in the value of our investment securities.

There are a few items that warrant some additional discussion and analysis to help in understanding our broader business and balance sheet dynamics.

First, the calculated margin declined by 11 basis points in the quarter. We estimate: 7 basis points of that was due to lower number of days this quarter, generating less income, and our simple margin calculation method in which each quarter, regardless of the number of days, gets the same one-quarter annualization factor; a further 2 basis points of the margin decline came from our reverse mortgage income, which as you know, can be volatile; and the last 2 basis points came from the impact of heavy competition on loan yields.

Switching to credit quality, our NPAs to total assets at 1.22 percent and total credit costs at $3.1 million were at good overall levels. While total credit costs were in line with guidance of $3 million to $3.5 million per quarter for 2014, they were moderately elevated from last quarter, primarily driven by two medium-sized relationships that went delinquent and were put on non-accrual status. As we've indicated, while credit quality and credit cost continued to trend down to pre-great recession levels, they can, in any quarter, be uneven.

Finally, as mentioned earlier: the first quarter of the year, winter months in general, and the harsher weather this year specifically, are impactful in a compounding way due to: the lower number of days to earn revenue; less activity occurring in the economy, affecting our particularly transaction-heavy, fee-based businesses; higher compensation and related costs that typically come with the start of a new year; and higher expenses from things like snow removal and utility costs. We estimate, in this quarter, as compared to the fourth quarter of 2013, that Net Interest Income was reduced by $650,000 for the two fewer days; compensation and related costs increased approximately $800,000 from employment taxes and 401(k) matching costs that cap-out over the course of the year; and the harsh winter increased our expenses by approximately $400,000. The impact on fee income is much harder to isolate, but based on our history, typically, core fee income in the first quarter is 5 percent to 7 percent lower than the fourth quarter (right now that equates to about $1 million to $1.4 million), and we expect would be at the high end of that range if it is a rougher winter.

We also expect most of these first-quarter impacts will recede as 2014 progresses, and with our continued good growth and the local economy showing increasing signs of strength, we look forward to a very good 2014.

Thank you, and at this point, we'd be happy to take your questions.

Operator: At this time, if you would like to ask a question, press star then the number one on your telephone keypad. We'll pause for just a moment to compile the Q&A roster.

And our first question comes from Catherine Mealor from KBW. Please go ahead.

Catherine Mealor: Hi, good afternoon, everybody.

Mark Turner: Good afternoon, Catherine.

Catherine Mealor: I wanted to see – you mentioned in the release and your remarks about how you're seeing a decline in your overall loan yields from increased competition. Can you give us a little bit of color behind generally where you're seeing loans coming off and then coming on your portfolio right now?

Rodger Levenson: Hi, Catherine. It's Rodger Levenson speaking.

Catherine Mealor: Hi Rodger.

Rodger Levenson: In terms of where we're seeing loans coming on, if you look at this past quarter, average loan yields for loans greater than $500,000, which is really the majority of our commercial business, came in at 4.3 percent on a weighted average basis. So that's right in line with what our overall yield has been and stands up very favorably compared to our peers. Obviously, our runoff is a little bit north of that in terms of the higher yielding loans that are running off, but that gap has been steadily declining and we're getting close to the point of equilibrium.

In terms of the competition, it's very intense. It's coming from across all sectors. One particular point I would highlight is one very large regional player in our market has been out with a heavy promo on up to $3 million owner-occupied commercial mortgage, five-year term, 20-year amortization at 3.69 percent, which is very aggressive and obviously compares differently to the business that we've been booking and has impacted our pricing decisions, somewhat. So it's – right now I'd call the pricing pressure intense.

Catherine Mealor: Got it. And so then how do we think about your NIM margin going forward? Do you still feel like there's a little bit of an upward bias towards your core margin?

Steve Fowle: Yes, Catherine, if you think about it, as we move into next quarter, it's a longer quarter, so that in itself will help with both the net interest income dollars and the margin calculations, but we don't pick up as many days as we lost going from Q4 to Q1. But additionally, if you think about what Rodger said about the commercial loan yields, there's still pressure, but the pressure should decrease as we're approaching an equilibrium to what our current portfolio yield is.

So the trends in terms of the downward pressure, should slow somewhat. But at the same time, we are expecting offsetting continued growth in our businesses, and as a result of that, continued improvement in balance sheet mix. That should help us out. So I'd anticipate upward trends from some more quantitative factors in Q1 and then some additional opportunity to pick up incremental increases and margin beyond that.

Catherine Mealor: OK. Very helpful, thank you.

Mark Turner: Thank you.

Operator: Thank you. And our next question comes from Jason O'Donnell from Merion Capital Group. Please go ahead.

Jason O'Donnell: Good afternoon.

Mark Turner: Good afternoon, Jason.

Jason O'Donnell: Rodger just given your commentary on the loan yield potentially stabilizing soon and you just shared with us some thoughts around the margin potentially increasing, is that something that is likely to be material or are you envisioning maybe just a few basis points of expansion as you look out over the next couple of quarter?

Steve Fowle: I'd anticipate gradual and slower: a few basis points, as opposed to larger chunks. But, again, the days of the month will help this coming quarter – I'm sorry, the days of the quarter.

Jason O'Donnell: Yes. And then just in terms of the outcome with respect to loan growth. This quarter was obviously pretty favorable just given the winter. How would you all characterize the loan pipeline at this point relative to where it was maybe last year at this time? Is it stronger, weaker, somewhere in the same range?

Rodger Levenson: Hi Jason, it's Rodger again. Our pipeline compared to this time last year is a little weaker. I really attribute that very much to the pricing competition, not that there aren’t overall opportunities out there, but we really only put things into that 90-day weighted average that we think have a high likelihood of closing. So we're a bit below where we were this time last year and where we tracked actually during most of the first quarter. So while I think we're still on track for a mid- to high single-digit loan growth for the year, this upcoming quarter could be a bit below that.

Jason O'Donnell: OK. Understood. And then on the – switching gears a little bit – on the non-interest income side, just thinking about the trajectory there, at least the core non-interest income, can you give us some color around your near-term expectations for the credit, debit card, and ATM line, do you expect that to bounce back a little bit into the second quarter? I know there are some moving parts in there given the impact of Cash Connect?

Rick Wright: It's a little hard to read because we're still trying to dissect a little bit about what's the impact of the winter versus the seasonal, but we clearly expect an improvement versus the first quarter and an improvement in the second quarter relative to 2013 second quarter.

Jason O'Donnell: OK. OK. Great. And then the last one and I'll hop out. On the mortgage banking side, do you expect to see a rebound there into the second quarter based on the pipeline you have currently, or is this a good run rate, all else equal in terms of rates?

Rick Wright: This is Rick Wright again. When, I answered the last question, I forgot to identify myself. Yes, we do expect some improvement. Looking at the pipeline over the last 30 days or so, it's improved quite a bit. At this point, we would say that we're expecting something in the $900,000 to $1 million range, so it would be an improvement.

The last couple of weeks would push me a little towards the top end of that, but we'll have to see how it goes. And I would say that we have turned to significant purchase money on the loan side as opposed to refis. It's running about 50 percent to 60 percent, so that's good news for us.

Mark Turner: And we're bucking the trend of the market out there because of our purchase of a Array Financial late last year, which is in a very good operation and primarily their business is – has been -- built on center of influence and the purchase money market business. So we're rebounding stronger in that than most that were more dependent on just refi business.

Jason O'Donnell: Great. That makes sense. Thanks a lot guys.

Mark Turner: Thank you.

Operator: Thank you. And our next question comes from Matt Schultheis from Boenning. Go ahead.

Matt Schultheis: Hi, good afternoon.

Mark Turner: Hey, Matt, good afternoon.

Matt Schultheis: A couple of quick questions, and I'm sorry if I missed this in my read of your press release. Were there any interest accrual reversals tied to the two larger loans that you put into non-accrual, and if so, how much were they?

Rodger Levenson: Yes, Matt, it's Rodger again. There were reversals – it was a modest amount, though. I don't have the exact basis point piece but it was a modest piece.

Steve Fowle: Just to add on to that a little bit, Matt, is that if you look at the quarter-to-quarter change net interest margin, in addition to the days of the quarter, if you look at the loan yields, particularly commercial, we did have a couple of hundred thousand of accounting adjustments in last quarter related to prepayments. So if you're trying to rationalize the difference quarter-to-quarter, it was less to do with things that impacted us negatively this quarter and more to things that impacted us positively last quarter.

Matt Schultheis: OK. Thank you. And can you add any color as to the nature of the loans that were moved into non-accrual – the two larger loan for $7 million and change?

Rodger Levenson: Yes, hi Matt. It's Rodger, again. These are two commercial real estate-related loans. One's in Cecil county Maryland, the other one is in Delaware County, Pennsylvania. Projects that are income-producing projects that suffered some vacancy and where the sponsor had some pressure in their overall global cash flow which caused them to go delinquent and subsequently non-accrual.

Matt Schultheis: Same sponsor?

Rodger Levenson: Two different sponsors. Totally unrelated.

Matt Schultheis: All right. Thank you very much. Have a good weekend.

Mark Turner: Thank you.

Operator: Thank you.

As a reminder, if you would like to pose a question at this time please press star followed by the number one on your telephone keypad. And our next question comes from Frank Schiraldi from Sandler O'Neill. Please go ahead.

Frank Schiraldi: Hi, guys.

Mark Turner: Hi, Frank

Frank Schiraldi: Most of my questions have been asked already, actually, but I'll just and one more on the margin, if I could. Steve, you mentioned on the last call that expected the NIM to improve slightly from 4Q levels. I took that to mean for the full year 2014. So if that's the case, is that still looking like a possibility here or does that reset downwards somewhat, given competition?

Steve Fowle: Yes, given the competition, and also the dynamics of the interest rates, I'm anticipating that we do improve through the year. My comment last time was about the overall year, not quarter-to-quarter. But I'd expect, as we recover the year, that we go out the last quarter similar to where we went out last year's last quarter, assuming we can continue to make the kind of growth in our balance sheet that we're expecting to make.

Frank Schiraldi: Got you. OK. That's all I had. Thank you.

Mark Turner: All right, thank you.

Operator: Thank you and I'm not showing any further questions. I would now like to turn the call back to Mark Turner for any further remarks.

Mark Turner: OK. Thanks again everyone for your time and attention. We will be on the road a couple times in the second quarter, and we look forward to seeing as many of you as possible then. Have a great weekend.

Operator: Ladies and gentlemen, thank you for participating in today's conference. This does conclude today's program. You may all disconnect. Everyone have a great day.

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