Operator: Greetings, and welcome to the Southwest Georgia Financial Corporation Third Quarter 2019 Financial Results Conference Call. At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Craig Mychajluk, Investor Relations. Thank you, sir. You may begin.

Craig Mychajluk: Thank you and good afternoon, everyone. We certainly appreciate your time today as well as your interest in Southwest Georgia Financial Corporation. Joining me on the call is DeWitt Drew, President and CEO, and Karen Boyd, Senior Vice President and Treasurer. We'll start with DeWitt's formal remarks on the third quarter and then we'll open up the call for Q&A. You should have a copy of our financial results that were released this morning and, if not, you can find them on our website at sgb.bank.

As you are aware, we may make some forward-looking statements during the formal discussion, as well as during the Q&A. These statements apply to future events that are subject to risks and uncertainties, as well as other factors that could cause actual results to differ materially from what is stated on today's call. These risks and uncertainties and other factors are provided in the earnings release, as well as with other documents filed by the company with the Securities and Exchange Commission. You can find these documents on our website or at SEC.gov.

With that, I'd like to turn the call over to DeWitt, to begin the discussion.

DeWitt Drew: Thank you, Craig. Good afternoon, everyone and thank you for being with us today. Our customer-focused strategy continues to differentiate us in our markets as we are seeing benefit from our investments and talent, geographic expansion and customer service enhancing initiatives. Loan and deposit growth continued at a healthy pace, despite some chaos in the local agricultural economy, and while costs to operate continue to be a challenge, we believe we are prudently managing our opportunity costs.

Net income was up 25% to $1.4 million and, on a per diluted share basis, earnings were $0.56, which was up $0.11 over the third quarter of last year. If you recall, in 2018, we achieved record results and, on a year-to-date basis, we're well on track to beat last year's earnings.

We're keenly focusing on managing our asset and liability mix. The rate environment is challenging and we're being disciplined in pricing both sides of the balance sheet. Efforts are paying off and we've been able to maintain a healthy net interest margin. At 4.08%, net interest margin is up 2 basis points since the second quarter of 2019.

The average cost of all the interest-bearing liabilities has increased 24 basis points year-over-year to 1.19%. Interest bearing deposit cost increased 30 basis points to 1.10% and we are less reliant on Federal Home Loan Bank (FHLB) funding.

Movements in interest rates this year gave us the opportunity to reposition a portion of our FHLB advances and the investment securities portfolio, which helped offset increased credit costs.

For the quarter, net interest income was up $432,000 to $5.2 million, which reflects higher interest and fees on loans of $676,000 partially offset by higher cost on interest bearing deposits of $284,000. Our provision expense was also higher at $130,000.

Non-interest income was up $214,000 to $1.2 million, primarily due to a gain on the sale of securities. Higher insurance revenue and higher debit card transactional fees were offset by smaller declines in other business lines.

On the expenses side, we're seeing increases across the board due to a tight labor market and recent strategic investments in talent and infrastructure necessary to organically grow the bank. However, total non-interest expense only increased $71,000 or less than 2% over last year's third quarter and declined 7% from the linked second quarter.

Strong revenue growth was the primary driver of the improvement in our efficiency ratio to 65.3% from 71% for the linked quarter.

Total assets at quarter end reached $548 million, an increase of 6%. Loans grew approximately 8% to $395 million, with contributions coming from each of our markets. While we have seen some softness this year, particularly in the agricultural space, we still have a solid pipeline and saw our third quarter loan portfolio increase more than 6% on an annualized basis.

With this growth, we continue to build a high-quality balance sheet and are mindful that exceptional credit metrics will give us a competitive advantage when the next recession comes. Our non-performing asset ratios improved over last year to 0.49% of total loans and 0.38% of total assets.

Our loan growth has continued to be funded by strong deposit gathering activities. Total deposits of $466 million were up more than 9% or approximately $40 million year-over-year. Importantly, more than a third of that growth was from noninterest-bearing transaction accounts. Also, given the success of our deposit gathering activities, we reduced our reliance on the Federal Home Loan Bank funding.

Deposit growth during the recent quarter was down slightly, but that was primarily due to seasonal fluctuations. We continue to believe that there are ample opportunities for us on the deposit side given disruptions in our industry and our customer-centric approach.

Turning to capital, the company consistently maintains regulatory capital ratios above the Federal well capitalized standard, including total risk-based capital ratio of 13.14%. Our book value per share grew 14% to $19.01 at quarter end. In September, we paid a quarterly cash dividend of $0.12 per common share and, for the year-to-date period, cash dividends have totaled $0.36, representing a 3% increase over last year's comparable period.

Our strong momentum continues to support our positive outlook. We are tracking to achieve record earnings this year and believe we are well-positioned to continue to capitalize on future growth opportunities.

That concludes my formal remarks and, with that, we'd like to open the call for any questions.

Operator: Thank you. We will now be conducting a question-and-answer session. [Operator Instructions] Our first question comes from the line of Michael Shay with Strategic Value Bank Partners. Please proceed with your question.

Michael Shay: Good afternoon. I know you mentioned the drop in the efficiency ratio and Q3 was really revenue driven, but I was hoping you could dig into the expense side a little bit more, specifically around what we could expect going forward from Q4 into 2020 as it relates to the overall spending across the board?

DeWitt Drew: Over the last two years, we’ve had a fairly large increase in our data processing expenses and that's transactional driven. Summer time is a very slow time for us. Our deposit balances are down, particularly those transactional accounts. We're in an agricultural area, so a lot of money goes into the ground and, additionally, the public funds accounts were less active. A lot of those funds have left the bank, so that line item is down a little bit during the summer. It typically starts to accelerate and increase again later in the year as those balances begin to come up. We are down about seven full-time equivalence since the end of the second quarter. We do have plans to replace a few of those; however, we don't have people in place just yet, but we're actively looking and. of course, that will be a small incremental increase for us when we do.

Overall, we're pleased with our operating expenses. We think we've done some other things that help us to operate a little bit more efficiently. We do know long term that we have to take that ratio down and we think that it's best to come down by achieving scale rather than cutting costs at this point in time. Growth is still very important to us.

Michael Shay: Okay. Switching over to the revenue and, really, on the margin front, what do you see looking forward to 2020 as you try to defend around some other things? So, securities and FHLB, any comments on those and what we can expect there.

DeWitt Drew: We think margin becomes a challenge for us as the lower rates go. We've done really well doing a few things on the asset side that you mentioned with respect to the securities portfolio doing a swap, taking a little bit of extension risk, but not much, and improving the overall yield on the portfolio. The issue on the asset side will become repricing balloon loans. Right now, we're getting a bump in rate as things roll off, but with just a little bit more decrease in overall interest rates, that advantage would go away.

We think we still have some advantage on the cost side on deposit liabilities. Overall deposit costs are close to 10 basis points down and we think that, during the last quarter of this year, we have an opportunity to make that even more. In general, interest rates are just lower and, competitively, we're seeing less pressure on the deposit side which we think is an advantage for us. However, I believe it will be hard to maintain that 4.08%.

We do see us a scenario where rates do maintain their current levels where we might actually pick up a little bit, but it's looking less and less likely that that's going to happen.

Michael Shay: Okay. Last question on my end, if I heard you correctly, if we get another rate cut from here, you expect deposit cost pressures to continue to follow to drop in suit into the rest of Q4?

DeWitt Drew: Yes, I think we're going to be good for the rest of this year; however, next year, there might be a little bit of a stretch for us to keep that low 4% net interest margin, but it looks very positive right now. We might be able to make it up on volume and we still have some room to increase our loan/deposit ratio a little bit. We'll have some increased provisions expansion. We continue to do that, but we think we still have some room to change our mix and work on it, at least keep net interest income growing.

Michael Shay: Okay. All right. Perfect. I think that's it from my end. Thanks for the update.

DeWitt Drew: Okay. Thanks, Michael.

Operator: [Operator Instructions] Thank you. Our next question comes from the line of Ross Haberman with RLH Investments. Please proceed with your question.

Ross Haberman: Good morning, gentlemen. I was wondering, do you have any specific plans for any new branches in the coming three to six months and are you actively looking for any additional lenders? Thank you.

DeWitt Drew: As far as new branches in three to six months, no, we are not. We tend to operate on a four- or five-year time frame rather than three to six months. We're fairly new to the Tifton market, which we think is a very nice market, and think we have a lot of potential there. Also, we are still growing in the Valdosta market at a pretty good clip. Additionally, we don't want to distract from those things that we've done strategically that we want to be successful at before we start looking to go to our next market, whatever that might be.

Ross Haberman: And just one follow-up. Generally, are those your best two economic markets or, if not, which ones are?

DeWitt Drew: The Valdosta-Lowndes County has the strongest growth prospects of the markets we're in and our Tifton market and Moultrie markets are equivalent. They're all slow growth relative to the rest of the country, but for South Georgia, for this part of the world, Valdosta is an attractive market. With respect to new lenders, we're modeling on trying to add two new lenders, one in Valdosta and one in Tifton, hopefully over the next 12 months.

Ross Haberman: Thank you. The best of luck.

DeWitt Drew: Okay. Thank you.

Operator: Mr. Drew, we have no further questions at this time. I would now like to turn the floor back over to you for closing comments.

DeWitt Drew: Okay. I just want to say thank you to everyone for joining us on the call. We appreciate your continued interest and support. Please feel free to reach out to us at any time and we look forward to talking with you again after our fourth quarter results. Again, thank you for participating and have a great day.

Operator: Ladies and gentlemen, this does conclude today's teleconference. You may disconnect your lines at this time. Thank you for your participation and have a wonderful day.