Southwest Georgia Financial Corporation
Fourth Quarter and Full Year 2018 Financial Results
January 22, 2019

Operator: Greetings, and welcome to the Southwest Georgia Financial Corporation Fourth Quarter and Full Year 2018 Financial Results. [Operator Instructions] As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Craig Mychajluk, Investor Relations for SGB. Thank you, Mr. Mychajluk. You may begin.

Craig Mychajluk: Thank you, and good afternoon, everyone. Certainly appreciate your time today as well as your interest in Southwest Georgia Financial Corporation. Joining me on the call is DeWitt Drew, our President and CEO, and Karen Boyd, our Senior Vice President and Treasurer. We'll start with DeWitt's formal remarks on the fourth quarter and full year; 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. If not, you can find them on our website at www.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. Over the last year, we continued to build out our infrastructure and invest in people in order to grow organically in the markets in which we currently operate. This translated into market share gains as we expanded and deepened relationships with existing customers, added high-quality new clients, and further penetrated the Tift County market as our new full-service banking center in Tifton helped cement our ability to be relationship bankers in that area.

These actions resulted in strong loan and deposit growth and, when combined with lower corporate tax rates, generated record earnings in 2018. Specifically, we achieved full year net income of $4.7 million, up 23%. On a per diluted share basis, earnings were $1.84, up $0.35. Even absent the impairment charge for the deferred tax assets in last year's fourth quarter, earnings for the year would still have been up $0.18 or 11%. For the fourth quarter, net income was $1.2 million or $0.46 per diluted share.

Core pre-tax income was up for both periods. Our core excludes gains and losses on the sale of securities or assets, gains from debt extinguishment, the change from closing our mortgage banking subsidiary, and changes to provision for loan losses. For the year, core was up $735,000, an increase of 14%. The quarterly increase was $53,000 or 3.5%.

Net interest margin did contract 14 basis points to 3.94% in the quarter and 10 basis points to 3.99% for the year. Those declines can be attributed to a decrease in the tax equivalency adjustment to our tax-free bond portfolio necessitated by lower tax rate as well as changes in the volume and rate paid on interest-bearing liabilities.

Our strong loan growth has expanded our net interest income, which was up 7% to $4.8 million in the quarter and up 8% to $18.6 million for the full year period. As expected, we took higher provisions in both periods due to the continued loan growth and our preparation for the Current Expected Credit Loss, or CECL, migration.

Total noninterest expense was up 10% and 5% in the fourth quarter and full year period, respectively. While we continue to be vigilant in managing expenses, there were a number of items that contributed to those increases. We had higher marketing cost around the new branch expansion, the introduction of the new interest-bearing business checking product, and have seen an elevated level of losses due to debit card fraud. We do expect those expenses to come down and be more in line with historical levels, but will experience increases in some data processing categories due to enterprise-wide pricing adjustments as our total assets exceed the $500 million level.

Total assets reached $535 million, an increase of 9% year-over-year. At $377 million, loans grew 14% for the year with growth present in all of our geographic regions. In particular, the Valdosta market continued to perform very well for us and, at year-end, held approximately 50% of the bank's total loans. The loan mix was stable and relatively unchanged, with it centered in real estate at about 75% of loans. Average total loans in the fourth quarter increased $42 million or 13%. With contributions coming from our entire footprint, our loan pipeline and originations remained strong and as diverse as is the portfolio.

With net charge-offs for the year at 13 basis points and nonperforming assets at 25 basis points, asset quality remains strong, even as we work through local challenges. As we mentioned last quarter, we have had three consecutive years with a tropical system moving through our market area, putting pressure on the agricultural industry; in particular, cotton and pecans. Further, trade disputes with China have also had an effect on both cotton and pecan markets. To date, our exposure has been limited and we think we're well positioned, and whatever problems and stresses develop, they are certainly manageable.

Our loan growth was funded by exceptionally strong deposit growth of 15% or nearly $59 million. The increasing rate environment and the introduction of our new interest-bearing business checking product continues to shape the deposit mix. Noninterest-bearing deposits declined $24 million, while interest-bearing deposits increased $83 million. Deposit costs were higher, but in line with our expectations. The average cost of interest-bearing deposits was 1.06% for the fourth quarter.

We continue to focus on relationship banking and have managed deposit pricing to attract and retain deposits to support our loan growth and to reduce our reliance on the Federal Home Loan Bank. Deposit growth exceeded loan growth and we were able to retire a significant amount of FHLB debt.

Due to record earnings and a solid capital position, we paid total dividends of $0.47 per share in 2018, up 7%. We've now paid a cash dividend for 90 consecutive years.

As we look out, the economic recovery from the great recession has gotten long in the tooth. Although we do not at this time see an impending recession, we do believe that growth will likely be slower next year.

Overall, our performance at SGB suggests that, in many ways, we're ‘on top’ right now, and smart money has, historically, prepared for the next recession while on top, and that's what we have begun to do. We will continue to make higher provisions to build up the reserve for loan losses and create a buffer for cleaning up weaker credits as they develop. We will also continue to be disciplined when pricing both loans and deposits; although, making sure we all remember that a quality relationship is more important than yield.

Lastly, as some of you may have seen, we recently announced the expected retirement of our Chief Operating Officer, John Cole, along with other leadership promotions that we believe will further bolster our bench strength. We have an incredibly talented and dedicated group in our lenders, support staff and management team, and the results we have achieved over the past year were largely due to the depth of talent throughout our organization. Our sights remain keenly focused on a successful 2019 and beyond.

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

Operator: Our first question comes from the line of Mike Shay with Strategic Value Bank Partners.

Mike Shay: I really have just two questions. One, more so on your investment focus for 2019 and beyond on the people, processes and products. Do you have any thoughts as to further building out the infrastructure base and the team within the market, so any list of things of that nature versus expansions to any new branches or more new direct banking centers like you just opened? And then, two, on the liability mix, do you see any further pressures on the deposit base? I know you instituted the new business checking product, but is there anything else that is effectively going to stem the tide from the pressures you're seeing there?

DeWitt Drew: Mike, thanks for participating today. On investments, right now, I'll say we're focused on keeping our ship in order. I don't see us doing anymore de novo expansion in 2019; although, the planning for that is certainly part of our strategy going forward. We have to make sure that we do well in Tifton and continue to do well in Valdosta. We think we have a lot of legs in Valdosta and room to grow, so I don't see more de novo expansion in 2019.

As far as further expansion in the markets we're in, we are actively looking for some more talent in Tifton, and we think that, if we find the right person, we will add to our staff there. We think there's a lot of opportunity there.

As far as deposit pressure, I don't think we got ahead of ourselves on deposit pricing. We were concerned about deposit betas and making sure the liquidity didn't go away as money markets ramped up and other establishments started paying up for deposits. I think the almost $60 million deposit growth last year was very encouraging and indicates that that pressure may not be as significant as we thought it would be at first. But it's going to be important to keep that liquidity going forward and continue to fund our loan pipeline, and we'd also like to continue to pay down our home loan bank debt a little bit, more in an effort to manage our capital ratios than anything else.

Operator: There are no further questions in the queue. I'd like to hand the call back to management for closing comments.

DeWitt Drew: I want to thank everyone, again, for participating and joining us on the call. We certainly appreciate your continued interest and support, and look forward to talking with you again after our first quarter 2019 results release. Again, thank you for participating, and have a great day.

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