S&P Global
Market Intelligence

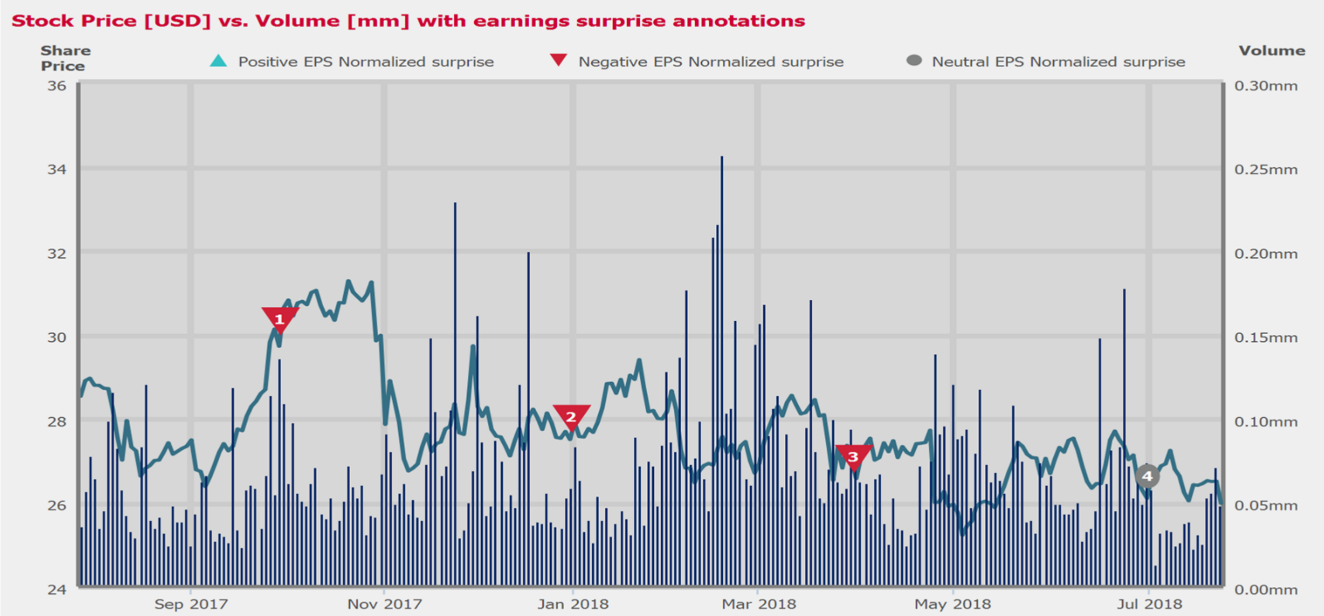
Flushing Financial Corporation
NasdaqGS:FFIC
FQ3 2018 Earnings Call Transcripts

Wednesday, October 24, 2018 1:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2018-			-FQ4 2018-	-FY 2018-	-FY 2019-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.48	0.54	▲12.50	0.49	1.84	1.93
Revenue (mm)	45.38	46.48	▲2.42	45.69	183.04	190.03

Currency: USD
Consensus as of Oct-24-2018 1:00 AM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ3 2017	0.44	0.37	▼(15.91 %)
FQ4 2017	0.42	0.33	▼(21.43 %)
FQ1 2018	0.44	0.37	▼(15.91 %)
FQ2 2018	0.48	0.49	●0.00 %

Table of Contents

Call Participants

EXECUTIVES

John R. Buran
President, CEO & Director

Susan K. Cullen
Senior EVP, Treasurer & CFO

ANALYSTS

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

Collyn Bement Gilbert
Keefe, Bruyette, & Woods, Inc., Research Division

Mark Thomas Fitzgibbon
Sandler O'Neill + Partners, L.P., Research Division

Steven Comery
G. Research, LLC

Presentation

Operator

Good morning, and welcome to Flushing Financial Corporation's Third Quarter 2018 Earnings Conference Call. Hosting the call today are John Buran, President and Chief Executive Officer; and Susan Cullen, Senior Executive Vice President, Treasurer and Chief Financial Officer.

Today's call is being recorded. [Operator Instructions]

A copy of the earnings press release and slide presentation that the company will be referencing today are available on its Investor Relations website at flushingbank.com.

Before we begin, the company would like to remind you that discussions during this call contain forward-looking statements made under the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. Such statements are subject to risks, uncertainties and other factors that may cause actual results to differ materially from those contained in any such statements. Such factors are included in the company's filings with the U.S. Securities and Exchange Commission. Flushing Financial Corporation does not undertake any obligation to update any forward-looking statements, except as required under applicable law.

During this call, references will be made to non-GAAP financial measures as supplemental measures to review and assess operating performance. These non-GAAP financial measures are not intended to be considered in isolation or as a substitute for the financial information prepared and presented in accordance with U.S. GAAP. For information about these non-GAAP measures and reconciliation to GAAP measures, please refer to the earnings release.

I'd now like to introduce John Buran, President and Chief Executive Officer, who will provide an overview of the strategy and results.

John R. Buran
President, CEO & Director

Thank you. Good morning, everyone, and thank you for joining us for our third quarter 2018 earnings call. Today, we hope to provide additional insight into our business strategy, sustainable competitive advantages and consistent positive earnings power.

I'll begin by walking you through our third quarter highlights and then provide an overview of the strategies we are executing to create long-term shareholder value. Then our CFO, Susan Cullen, will review our financial performance in greater detail. After our prepared remarks, Susan and I will address your questions.

Beginning on Slide 3. Third quarter '18 GAAP diluted EPS was $0.61 and core diluted EPS was $0.54. Core earnings were positively impacted by the reversal of a previously recorded tax liability of approximately $2 million. The difference between GAAP and core earnings per share is attributable to approximately $2 million in gains from life insurance proceeds.

Net interest income of nearly $42 million was down modestly quarter-over-quarter and year-over-year due to net interest margin pressure, driven by higher funding cost. The cost of funds increased 22 basis points quarter-over-quarter and 48 basis points year-over-year as the Federal Reserve has raised rates by 100 basis points since the third quarter of 2017.

The competition for deposits this quarter was especially strong in the municipal sector. Overall, we expect continued competition for deposits and additional compression on the net interest margin through 2019. We are pleased with our ability to generate strong earnings growth and return on average equity of nearly 13% and core return on average equity of over 11% despite continued margin pressure.

Our strategic focus of emphasizing rate over volume and reducing our liability-sensitive position has resulted in net loan growth of approximately 1% from the linked quarter. Similar to the prior quarter, we allowed $62 million of participations with another financial institution to prepay as the rates offered through the refinancing process did not meet our criteria. Year-to-date, we have allowed approximately $139 million of participations to repay rather than refinance at a rate below our criteria.

During the quarter, approximately 70% of our new loans and 40% of our new investment securities were adjustable rate products, allowing us to reduce future compression on the net interest margin. Also, approximately $450 million of forward swaps entered in late 2017 have provided benefit for the first time this quarter. We expect these swaps to increasingly benefit our net interest margin as rates rise.

The swaps, coupled with the extension of the maturity of liabilities, has reduced our liability-sensitive position. The yield on the loan portfolio increased 21 basis points from the linked quarter, representing successful execution of our strategic objectives. Also, the yield on mortgage loan originations increased 8 basis points from the linked quarter.

However, the yield on all new loan originations decreased 8 basis points during the quarter due to the initial rate recorded on certain adjustable rate C&I loans. Importantly, these loans have an average rate reset of 3 months. Over the past 5 quarters, C&I loans represent 39% of new loan originations, which are primarily adjustable rate loans.

As we have previously disclosed, we have approximately $2 billion of loans repricing through 2020, of which $127 million in mortgage loans have repriced up an average of 68 basis points during the third quarter. In addition, the pipeline remains strong at $355 million with an average yield of 4.68% compared to $323 million at 4.67% in the linked quarter.

The loan-to-deposit ratio improved to 114% from 116%, largely due to retail deposits increasing $106 million quarter-over-quarter. A prominent feature in the growth of retail deposits is our Win Flushing program, which focuses on increasing our deposit market share in the Asian community in Flushing, Queens. Through the third quarter, we have captured over $100 million in deposit growth through this program and remain on pace to add $160 million in deposits by the end of the first quarter of '19.

Central to the Win Flushing program has been the conversion of Flushing branches to the Universal Banker model, permitting staff to spend more time with customers. In the branches converted, we have seen balances grow over 15% and have experienced an increase of 120% in transactions processed at an ATM, reducing our customer's reliance on tellers. As previously discussed, we remain committed to improving our overall expense scalability and efficiency by completing the remaining branch conversions to the Universal Banker model by the end of 2019 and opening a branch in Chinatown, Manhattan in the fourth quarter of 2018.

Credit quality of our portfolio remains pristine. At the end of the third quarter, nonperforming loans were just 24 basis points of gross loans, and nonperforming assets were only 19 basis points of total assets. Nonperforming loans totaled less than $13 million in the third quarter, a decrease of 15% quarter-over-quarter and 9% year-over-year.

Referring to Slide 4, we remain focused on the following key areas: exceeding customer expectations, enhancing earnings power, strengthening our commercial bank balance sheet and maintaining our strong risk management philosophy.

Our sustainable competitive advantages include our ongoing focus on developing and maintaining a multilingual branch staff to serve our diverse customers in the New York City market area. The Asian banking market surrounding our branches has very attractive business dynamics, including a high degree of savings, available deposits and a significant number of small business owners.

We have a strong focus on this community where we have over $600 million in deposits. These deposits have a lower cost of funds than our total cost of funds. Our Win Flushing campaign is focused on further capitalizing on this market through market knowledge and understanding of customer needs.

Overall, we remain very well positioned to deliver profitable growth and long-term value to our shareholders as we continue to execute on our strategic objectives, which is summarized on Slide 5: increase core deposits and continue to improve funding mix, manage net interest income by leveraging loan pricing opportunities, enhance core earnings power by include -- improving scalability and efficiency, manage credit risk and to remain well capitalized under all stress test scenarios.

During the third quarter, we repurchased nearly 300,000 treasury shares at an average cost of $25.58 per share. And as of September 30, 2018, approximately 509,000 shares remain under the current authorized stock repurchase program, which has no expiration or maximum dollar limit.

Overall, we remain well capitalized and our focus on our strategic objectives enable us to further deliver profitable growth and long-term value to our shareholders.

Now I'll turn the call over to Susan to discuss the quarter's financial results in greater detail.

Susan K. Cullen
Senior EVP, Treasurer & CFO

Thank you, John. I'll begin on Slide 6. Total loans are $5.4 billion, up nearly 1% quarter-over-quarter and 6% from the third quarter of 2017 as we continue to focus on the origination of multifamily, commercial real estate and commercial business loans with full banking relationship. These originations totaled 89% of total loan production for the third quarter of 2018.

We continue to diversify our loan portfolio as C&I originations for the quarter were 43% of total originations and 39% over the past 5 quarters. This has resulted in commercial business balances growing over 25% during the same period to approximately 16% of gross loans as of September 30, 2018.

The growth in the C&I portfolio offers several advantages to the company, primarily continued diversification of the loan portfolio. And as these are primarily adjustable rate loans, the yield offers more protection in a rising rate environment. Overall, total loan growth is on pace to meet the lower end of the expected loan growth while we continue to emphasize rate over volume.

At September 30, our loan pipeline was strong and totaled $355 million, which is up from last quarter. The composition of the pipeline was 75% adjustable rate product or $265 million of the pipeline and 25% fixed rate. The interest rate of the mortgage loan of the pipeline increased slightly from last quarter to 4.68%.

The loan-to-value on our real estate portfolio at quarter end remains a modest 39%, and the debt service coverage ratio for the current quarter's originations of multifamily, commercial real estate and 1-4 family mixed-use loans is 173%.

We underwrite and stress-test each individual loan using a cap rate in excess of the mid-5% range.

Slide 7 highlights the composition of our funding mix. As funding has grown over the years, the percentage related to CDs and borrowings has decreased. When the need arises to access the wholesale funding markets, we can ladder out liabilities for longer terms, which is an advantage. Core deposits increased 0.40% quarter-over-quarter and approximately 4% year-over-year and totaled 66% of all deposits at September 30, 2018, compared to just 37% at December 31, 2006.

On Slide 8, you see the deposits increased 2% over quarter-over-quarter and 6% year-over-year. Growth was primarily driven by money market CD and noninterest-bearing accounts. We continue to focus on the growth of core deposits with an emphasis on noninterest-bearing deposit accounts, which increased 10% year-over-year. Noninterest-bearing deposits of nearly $400 million represent 9% of total deposits.

We continue to see rate pressure with increased competition for deposits. The quarterly cost of deposits increased 22 basis points from the prior quarter. As John noted, the competition for deposits this quarter was especially tough in the municipal sector as the cost of NOW and money market accounts increased 39 basis points and 32 basis points. We remain disciplined in terms of deposit pricing while remaining competitive in our markets.

Turning to Slide 9. Net interest income for the third quarter of 2018 was $42 million, down modestly quarter-over-quarter and year-over-year. The net interest margin at 2.71% decreased 5 basis points quarter-over-quarter and 19 basis points year-over-year. Excluding prepayment penalty income and recovered interest from delinquent loans, net interest margin would have been 2.51%, a decline of 13 basis points quarter-over-quarter and 26 basis points year-over-year. We expect continued margin pressure through 2019.

As John noted in his remarks, we have about $2 billion of loans repricing through 2020, of which $127 million mortgage loans have repriced up an average of 68 basis points during the third quarter from an average rate of 4.56% to 5.24%. Our overall cost of funds for this quarter was 1.63%, an increase of 22 basis points quarter-over-quarter and 48 basis points year-over-year.

In order to partially mitigate the increase in the cost of funds, we have taken the following steps, which are summarized on Slide 10. For the fifth consecutive quarter, the yield on loan originations have exceeded the quarterly yield on the loan portfolio, net of prepayment penalties and recovered interest from delinquent loans.

We entered in forward swaps totaling approximately $450 million, of which approximately $350 million have been funded as of September 30, 2018. The forward swaps provided a benefit for the first time in the current quarter's net interest margin, and we project these swaps will enhance earnings as rates continue to rise.

Loan originations yields have increased 24 basis points from the third quarter of 2017. And as previously mentioned, originations of commercial business loans which are primarily adjustable rate loans, totaled 43% in the current quarter and now compromise 16% of the loan portfolio.

We actively managed funding costs and continue to evaluate strategies to mitigate our liability-sensitive balance sheet. While net interest margin will likely remain pressured, we will continue to focus on driving net interest income by executing on the previously noted steps, coupled with leveraging loan pricing opportunities and portfolio mix.

On Slide 11, we reported noninterest income for the third quarter of 2018 of $5 million and core noninterest income was $2.9 million, which excludes the net loss of fair value adjustment and the $2 million gain from life insurance proceeds. The core decrease quarter-over-quarter was primarily driven by a reduction in the net gain on sale of loans.

Moving to Slide 12, we project 2018 annual expenses to increase approximately 3% to 5% from 2017, driven by the growth of the bank. Overall, the efficiency ratio was just over 61% in the third quarter of 2018 compared to 60% in the second quarter of 2018 and 57% in the third quarter of 2017. As previously discussed, our long-term goal is to achieve an efficiency ratio in the low to mid-50s.

We remain focused on continuous improvement and new opportunities in our operations for efficiency gains. The increase in compensation expense for the quarter was due to the acceleration of benefits due to an officer's death and normal accrual adjustments.

Regarding taxes, the effective tax rate was just under 10% for the third quarter, benefiting from the release of a previously accrued tax liability. We anticipate the effective tax rate to increase to approximately 21% in the fourth quarter and approximately 19% for the full year.

Now turning to credit quality on Slide 13. Our credit metrics remained excellent this quarter. As a reminder, we are a historical seller of nonperforming credits and record charge-offs early in the delinquency process. As you can see, our improving credit quality metrics results in our coverage ratio increasing to 161% from 112% as of December 31, 2017.

The average loan-to-value of our nonperforming real estate loans was approximately 35% based upon the value of underlying collateral and origination, and we do not adjust appraisal for increases. Given the low loan-to-value associated with the nonperforming real estate loans, we do not foresee an increase to related expenses. Looking forward, with expected loan growth, we anticipate recording provision for loan losses proportionate with that growth in future quarters to maintain an adequate ratio.

Moving to Slide 14, nonperforming loans were just under $13 million, down 15% quarter-over-quarter and 9% year-over-year as credit quality remains one of our core strengths. We did not record a provision for loan losses in the third quarter due to the strong credit quality. Net recoveries of $89,000 in the third quarter reflect our conservative underwriting and diligence in the collection process.

Slide 15 shows 90-day delinquencies as a percentage of loans originated by year. Here, you can see the results of our strong underwriting discipline as there are only 3 loans delinquent greater than 90 days for vintage years after 2009. Overall, our credit quality remains pristine.

With that, I'll turn it back to John for some closing comments.

John R. Buran
President, CEO & Director

Thank you, Susan. On Slide 16, I'd like to conclude by reviewing why we believe we are well positioned for continued strategic and profitable growth.

Our vision is to be the preeminent community financial services company in our multicultural market area by exceeding customer expectations and leveraging our strong banking relationships. The New York City market, with its strong Asian customer base in Flushing, continues to represent a significant opportunity for us.

We remain focused on providing a superior and consistent experience at every touch point for our customers through innovation, quality service and personalized attention. We have a strong foundation with attractive markets and customers, a proven track record and an experienced leadership team to execute our strategy.

In conclusion, our strong balance sheet, risk management philosophy, capital levels, ability to grow deposits, investments in talent, innovation and cybersecurity all position the company very well to deliver profitable growth and long-term value to our shareholders.
We will now open it up to questions. Operator, I'll turn it over to you.

Question and Answer

Operator

[Operator Instructions] Our first question today will come from Mark Fitzgibbon of Sandler O'Neill.

Mark Thomas Fitzgibbon
Sandler O'Neill + Partners, L.P., Research Division

Susan, just to clarify, you said in your comments that you expect NIM pressure to persist through 2019. Do you think -- based on what you see today, do you think that the magnitude of the margin compression in each subsequent quarter will look similar to what we saw this quarter? Or does it -- do you think it alleviates as we get further into '19?

Susan K. Cullen
Senior EVP, Treasurer & CFO

I think it's going to be driven by the betas that we see on the deposit pricing. We're seeing the loans start to turn the corner, but we've seen more and more pressure on our deposit pricing. So the beta is really going to be the driver of our NIM compression.

Mark Thomas Fitzgibbon
Sandler O'Neill + Partners, L.P., Research Division

Okay. And then at what CD term are you having the most success in bringing new money in and at what sort of rate?

Susan K. Cullen
Senior EVP, Treasurer & CFO

It's about the 9 month, 2.40%.

Mark Thomas Fitzgibbon
Sandler O'Neill + Partners, L.P., Research Division

In around 2.40%, okay.

Susan K. Cullen
Senior EVP, Treasurer & CFO

Right.

Mark Thomas Fitzgibbon
Sandler O'Neill + Partners, L.P., Research Division

And then I know you touched on this a little bit in your comments and certainly, your credit quality is outstanding. But the loan loss reserve to loan ratio, it continues to skinny down at 38 basis points. It looks optically low. When do you think we'd see a resumption of provisioning?

Susan K. Cullen
Senior EVP, Treasurer & CFO

Well, we've evaluated every quarter, Mark, and we had some net recoveries this quarter that masked it a little bit. The loan growth, unfortunately, has been a little on the skinny side, as you say. We've been at 38 basis points for a couple of quarters now. We have the low LTVs in our commercial portfolio, commercial real estate portfolio. We expect normalizing it soon in the next couple of quarters, given loan growth, as we said.

Operator

And our next question will come from Steve Comery of G. Research.

Steven Comery
G. Research, LLC

I was wondering if maybe you could give a little more color on sort of the C&I rates in the quarter and explain kind of why the initial rate was lower. The magnitude there looks pretty significantly, 4.50% versus 4.9% in the previous quarter.

John R. Buran
President, CEO & Director

So some of them were priced at a -- spread over LIBOR, most of them are priced at a spread over LIBOR. And this is a competitive market, and as a result, the initial rates are a little bit less than, let's say, our initial rates on commercial real estate are. But over time, we expect that we will continue to see some protection, let's say, on the margin due to the fixing of these spreads versus LIBOR. In addition, we're focused on in the C&I business that has high credit quality. So obviously, that makes the rates a little bit more competitive than what we would normally see in that C&I portfolio.

Steven Comery
G. Research, LLC

Okay. Okay, fair enough. And then kind of noninterest-bearing deposits on a period end basis, those were up pretty nicely. Is there anything differently you guys are doing there, any more business you're getting from C&I? What's coming through there?

John R. Buran
President, CEO & Director

So it is C&I, but I've got to say that we've got a lot going on in the Win Flushing program. And we're very excited about that. The results are strong, over $100 million of additional deposits. And despite the fact that some of them are oriented toward obviously CDs, there is quite a bit of noninterest-bearing accounts coming in associated with the new businesses that we're bringing in, in the Flushing marketplace particularly.

Steven Comery
G. Research, LLC

Okay. So it doesn't sound like this is a different strategy, just kind of things are starting to pay off at Win Flushing and C&I lending?

John R. Buran
President, CEO & Director

Yes. I think what we're finding is that we've hit upon a method of going into a market in a more concentrated manner and achieving some very nice results. I mean, we expect to pick up a full point of market share in this -- in a $16 billion market. So it's pretty significant. And we also feel that we can take these learnings and move them out to other potential ethnic areas.

Steven Comery
G. Research, LLC

Okay. Okay, very good. And if I can switch gears, more to go to the CRE portfolio, I mean, it looks like -- I mean, growth was kind of negative in the quarter in those categories on a period end basis. Is anything changing there? Or is that still sort of less attractive to you than C&I is at this point?

John R. Buran
President, CEO & Director

It's competitive obviously. Remind you again that we did have, over the course of the 9 months, over $139 million of participations that we chose not to be a part of because the yields are in the 3 areas. So we're really focused on continuing to diversify our portfolio. And of course, we do like real estate. We do think there are still opportunities in commercial real estate. But if the new loan yields are not meeting our expectations, we'd rather leave the powder dry for a better day. And we fortunately have been in the C&I business for over 10 years, and as a result, we've got a track record there. We brought new people along to help us grow the portfolio. So we've got the ability to increase in a -- in an attractive market and an attractive product set. And frankly, if real estate comes back and the yields is to our liking, we'll be happy to jump in again. But until that time, we'll concentrate a little bit more on the C&I, which was about 39% of our originations for the year.

Steven Comery
G. Research, LLC

Okay. And then just one more for me, if I may. You guys are obviously active repurchasing during the quarter. In the past, I know this is certainly outdated a couple of years ago, you talked about like the $20 level being sort of extremely attractive to repurchase the stock. Maybe if you just give some kind of updated guidance about sort of your appetite for repurchases, whether or not you expect to use up your authorization and ask for more there.

Susan K. Cullen
Senior EVP, Treasurer & CFO

We anticipate opportunistically purchasing in the market as the market presents itself to allow us to do that. We do anticipate using up our full allotment that the board gave us. I can't give you any indication of what the time frame over which we will use that, but we do intend on using it at all.

Operator

Our next question will come from Collyn Gilbert of KBW.

Collyn Bement Gilbert
Keefe, Bruyette, & Woods, Inc., Research Division

John, just to get back to your comment on the fact that you guys chose not to be a part of the slug of the CRE books that you allotted to reprice elsewhere. Just curious, you had mentioned in the 3% range, who's financing those? Are those traditional bank lenders or non-bank lenders?

John R. Buran
President, CEO & Director

Traditional bank lenders.

Collyn Bement Gilbert
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. And then I guess, along those lines, 2 questions. One is, Susan, you had indicated that you're kind of expecting the loan growth to be at the lower end of your targeted range, and I apologize if you said what that was. But just curious now what you're thinking in terms of all-in loan growth for 2019.

Susan K. Cullen
Senior EVP, Treasurer & CFO

We're probably looking around the 6% range.

Collyn Bement Gilbert
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. And that slide is powerful when you show kind of where your current portfolio yield is and where you think that, that repricing rate could go. Do you see the risk in similar dynamics happening next year where these credits can just refinance at much lower levels elsewhere and you maybe won't participate in retaining those loans?

John R. Buran
President, CEO & Director

So remember, there's a cost associated with not doing this general role. So where we are today is that -- those customers would have to go out and get new appraisals. They'd have new legal fees, the -- so there's a whole host of cost associated with that. Now we may not make every penny on the 6% that we're looking at for 2019 and 2020, but we do think we've got a significant amount of leverage and we expect to utilize that. And as I said, we've got other opportunities to grow the portfolio if necessary. In addition, we firmly believe that other lenders who maybe undercutting pricing now will ultimately have to increase rates, which would make our position better.

Collyn Bement Gilbert
Keefe, Bruyette, & Woods, Inc., Research Division

Okay, okay. That's helpful. And then just on the deposit side, what are you anticipating kind of for overall deposit growth rates for next year?

John R. Buran
President, CEO & Director

We're thinking at around the 10% area.

Collyn Bement Gilbert
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. And do you have a sense of what -- of the new deposits that came in this quarter or that have come in year-to-date, how much of that is new customers versus current customers just shifting out of the savings or the money market into those CDs?

John R. Buran
President, CEO & Director

We think, given what's been happening in Flushing, that we're getting a few more new customers coming in. There's clearly much more -- I'd give you a perfect example. We did a -- we recently did a business blitz in the Flushing market. And although we're a still relatively small bank in that market, people knew us. And so I think that the recognition of the name and the recognition that we're doing something special in that market has taken hold. So we think we're getting more new customers. I mean, it appears that way, for sure.

Collyn Bement Gilbert
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. And then just on the noninterest-bearing deposit side, you had indicated it increased 10% year-over-year and it's 9% of the total. Where do you think that segment can continue to go?

John R. Buran
President, CEO & Director

I think we have some opportunity there. We -- again, we've clearly been successful in this one segment of the market. We're doing more C&I business, which, of course, brings more DDA with it. So I think those factors contribute to some positive growth in the noninterest-bearing area. So it's not an area that we've had a lot success of in, in the past, but clearly, the 11% -- 10%, 11% that we've gotten over the course of the last 12 months has made us more confident.

Collyn Bement Gilbert
Keefe, Bruyette, & Woods, Inc., Research Division

Okay, okay. And just -- so kind of looking at all of this broadly, I think if we assume, and I haven't run the numbers, but continuing NIM compression into '19 and just this slower loan growth, I presume we're going to see some savings obviously come through from the branch, sort of Universal Banker, but it seems like earnings are maybe just kind of running to be flat, if not down in '19. And just curious where you kind of see the levers to pull that. I mean, is it going to be -- and again, Susan, I know you had indicated the beta -- the provision starts to normalize, so maybe you won't get an offset there. I don't know if -- how you're thinking about the tax rate. But just trying to get a sense of maybe where you see some offsets coming from what will likely be flat to perhaps down net interest income growth or perhaps you're not seeing it that way.

John R. Buran
President, CEO & Director

Well, we think we got -- we think that one of the things that held back loan growth this particular year was that $139 million that we did not do in real estate participations. So we don't foresee that occurring again, that's for sure. And I think there's some additional expense opportunities that we can pick up over the course of the year as well. So that, in association with the role on the yields that we just discussed from 4 -- from a 4-handle to roughly a 6-handle in 2019, the additional C&I business that now floats over -- moves in LIBOR, and the swaps that we have, which, for the first time this quarter, have contributed positively to our NIM. So those are kind of the offsets to the margin pressures, the kind of generic margin pressure that we have as a result of the balance sheet.

Susan K. Cullen
Senior EVP, Treasurer & CFO

And Collyn, as we've said in the past, we'll again opportunistically look at other derivative-type transactions that would give us protection, additional protection in a rising rate environment, so we'd had that lever that we may be able to pull as well.

Operator

[Operator Instructions] Our next question will come from Brody Preston of Piper Jaffray.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

I guess, I just want to go back to the participations real quick. Are those multifamily loans or what asset class are those?

John R. Buran
President, CEO & Director

Sorry, we didn't get the question.

Susan K. Cullen
Senior EVP, Treasurer & CFO

We're having trouble hearing you, Brody.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

Yes, sorry about that. On the participations, I just want to know what asset class they were.

John R. Buran
President, CEO & Director

Well, multi, multifamily.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

And is that in market...

John R. Buran
President, CEO & Director

Yes.

Broderick Dyer Preston

Piper Jaffray Companies, Research Division

Doing those with?

John R. Buran
President, CEO & Director

It's in-market product. It's an in-market product in an in-market bank.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

Okay. All right, great. I guess, I just want to touch on credit real quick. I appreciate the fact that you guys have really pristine credit quality, and I guess, maybe the growth outlook is a little slower. But given how well you guys have been doing growing the C&I part of the portfolio, I guess, I wanted to get a sense for how you provision for that segment of the portfolio.

Susan K. Cullen
Senior EVP, Treasurer & CFO

Well, we provision for that segment like the other segments. We look at the collateral we have and/or use a discounted cash flow analysis to determine if there's any impairment and loss to be recognized.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

Okay. Is there -- do you have like sort of an average provision that you sort of apply to that portfolio?

Susan K. Cullen
Senior EVP, Treasurer & CFO

Well, we take our historical 3-year charge-offs in that and adjust for qualitative factors that are outlined in the inter-agency statement. We don't -- I don't want to give out what our percentages are for our competition's sake. But yes, we do have numbers and we look at them and we apply those and compare it to our balances and the discount cash flows and the collateral for impaired loans.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

Okay, great. And then I know the tax rate guide for 2019 -- for the 4Q is 21%. Is that sort of the run rate you expect moving forward?

Susan K. Cullen
Senior EVP, Treasurer & CFO

No, we haven't finalized all of our 2019. Again, we're refining that as we work through the budgeting process. As I'm sitting here right now, that would be a good estimate, but that's subject to change.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

Okay, great. And then in the release, you had mentioned you did have some classified assets that were still performing and still accruing, but you had put them sort of in the classified just given the trips on covenants. I wanted to get a better sense, I guess, maybe without going into specifics for those loans, but what are some of the typical covenants that you have within your various CRE and C&I loans?

John R. Buran
President, CEO & Director

So it might be a leverage covenant that was violated, let's say. We typically have a variety of liquidity leverage covenants with respect to the amount of capital that owners can take out of a -- out of the company at any given point in time. Obviously, we've got income and also reporting. So these are the kind of things that we generally put into reporting delays. These are the kind of things that we typically put in as covenants.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

Okay, great. And I guess, you read a bunch of articles that -- with larger loans sort of the proliferation of a cov-lite type of loan. And I wanted to get a sense for -- if you've seen any of that for maybe some of your type of clients, your size of clients. Are they coming to you expecting maybe fewer covenants than they have in the past?

John R. Buran
President, CEO & Director

So the market's competitive, for sure, and I'll kind of bring you back to the comment I made earlier about pricing versus credit quality. The pricing has been tight, and we're much more comfortable taking on tight pricing than loose credit criteria or loose covenants. So we try and stay away from overleveraged companies or more -- companies that -- or a range with such a light on covenants. We'd sooner take a little bit of -- a little bit less in terms of yield on the credit -- on the floating rate loans but get a better quality credit.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

Okay. Okay, that makes sense. I guess, the loan-to-value ratio on a lot of your real estate loans is pretty low. I think it's in like the 40% type of range. And so I wanted to get an idea as to -- I guess, are the borrowers bringing 60% down for that or like of their own equity? Or how are your borrowers sort of financing that 60%? Is it all out of pocket? Or are they getting maybe some debt to do that?

John R. Buran
President, CEO & Director

These may be refis, in many cases. And then we also tend to bank real estate owners and real estate investors that have been in the business for a long time and have a track record. And anybody who's been in the business for a long time doesn't typically put a lot of leverage on in their portfolio.

Susan K. Cullen
Senior EVP, Treasurer & CFO

I'd just like to remind you, Brody, that we don't adjust the denominator on those. Those are the loan-to-value calculations. That's loan-to-value at origination, wherever we've had an update. We're not taking the old appraisals when we originated the loan and increasing it for rates, indexes in this market area.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

Okay, so that's based off older -- the previous appraisal value?

Susan K. Cullen
Senior EVP, Treasurer & CFO

Original appraisal.

John R. Buran
President, CEO & Director

Yes, the original appraisal. I mean, if we refi it and get a new appraisal, we'll adjust then. But we don't adjust it year-over-year because prices are going up in Manhattan or in Brooklyn.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

Okay. All right, so that -- the net loan-to-value ratio could be even more then?

Susan K. Cullen
Senior EVP, Treasurer & CFO

Correct, could be.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

All right, that's good. And then I just want to go back to the pipeline. The pipelines picked up here relative to last quarter and the yield has a little bit too. I just want to get a sense for how you define your pipeline. Are those loans that you have term sheets out on?

John R. Buran
President, CEO & Director

Usually, there's -- there's usually some cash on the line. So as a matter of fact, there's always some cash on the line in these particular instances. So our real estate portfolio, somebody has put down money to start our processing.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

Okay, so the pull-through rate on that portfolio should be relatively high then, right?

John R. Buran
President, CEO & Director

Yes, that's -- yes, it is. It is.

Broderick Dyer Preston
Piper Jaffray Companies, Research Division

Okay. And then I appreciate that you guys typically have some seasonality within some of your deposit categories in the third quarter, driven by municipalities. But this year, the NOW seasonality was much larger, much greater than past years and you saw a really, really big inflow into money markets. And so I wanted to understand, is that a bit of a mix shift from your typical municipal clients or is there something else going on there?

John R. Buran
President, CEO & Director

No. I think it's fairly typical in terms of the seasonal patterns. Sometimes you get a few weeks on or off the typical pattern, but we're now in the area where in December, the money markets will be down a little bit -- the NOW accounts rather will be down a little bit, and then they'll come back very, very strong in January. So we had a slight build -- we get a slight build in the third quarter, reduce this a little bit in the fourth quarter and then comes back very strong in the first quarter. So that's typically what we see.

Operator

Ladies and gentlemen, this will conclude our question-and-answer session. At this time, I'd like to turn the conference back over to John Buran for any closing remarks.

John R. Buran
President, CEO & Director

Yes, thank you very much. So I think the thing that I'd like the investors to keep in mind about the company, and I think it's something that people have been with us a long time know. We run the company on a long-term basis. Obviously, we have the balance sheet that we have, it's a liability-sensitive balance sheet. But we're taking all measures that we possibly can to increase our opportunities for additional yield in loans while we're trying to control our funding cost.

So we've got a few things going on that are moving us in the right direction. And I think if you look at banks with similar balance sheets, I think you'll recognize that we have some opportunities due to diversification and situations that we've put in place in terms of hedging strategies that will put us in a position to turn the corner that leaves us good as most, if possibly better.

So thank you all for your attention. And if you have any other questions, feel free to give us a call. Thank you.

Susan K. Cullen
Senior EVP, Treasurer & CFO

Thank you.

Operator
Ladies and gentlemen, the conference has now concluded. Thank you for attending today's presentation, you may now disconnect your lines.