

Five Star Bancorp

First Quarterly 2024 Earnings

Tuesday, April 30, 2024, 1:00 PM Eastern

CORPORATE PARTICIPANTS

James Beckwith - *President and CEO*

Heather Luck - *Senior Vice President and CFO*

PRESENTATION

Operator

Welcome to the Five Star Bancorp First Quarter Earnings Webcast. Please note, this is a closed conference call, and you are encouraged to listen via the webcast.

After today's presentation, there will be an opportunity for those provided with a dial-in number to ask questions. To ask a question, you may press star, then one on your telephone keypad. To withdraw your question, please press star, then two.

Before we get started, let me remind you that today's meeting will include some forward-looking statements within the meaning of applicable securities laws. These forward-looking statements relate to, among other things, current plans, expectations, events and industry trends that may affect the company's future operating results and financial position. Such statements involve risks and uncertainties, and future activities and results may differ materially from these expectations.

For a more complete discussion of the risks and uncertainties that may cause actual results to differ materially from the company's forward-looking statements, please see the company's annual report on Form 10-K for the year ended December 31st, 2023, and in particular, the information set forth in Item 1A, Risk Factors.

Please refer to slide two of the presentation, which includes disclaimers regarding forward-looking statements, industry data and non-GAAP financial information included in this presentation. Reconciliations of non-GAAP financial measures to their most directly comparable GAAP figures are included in the appendix to the presentation. Please note, this event is being recorded.

I would now like to turn the presentation over to James Beckwith, Five Star Bancorp's President and CEO. Please go ahead.

James Beckwith

Thank you for joining us to review Five Star Bancorp's financial results for the first quarter of 2024. Joining me today is Heather Luck, Senior Vice President and Chief Financial Officer.

Our comments today will refer to the financial information that was included in the earnings announcement released yesterday. To obtain a copy of the release, please visit our website at fivestarbancorp.com and click on the Investor Relations tab.

Our organic growth story continued in the first quarter with the announcement of our underwritten public offering of 3,450,000 shares of the bank's common stock and underwriters' option to purchase up to an additional 517,500 shares with the intention of using the net proceeds for general corporate purposes, to support our continued growth and for working capital.

We also added five more seasoned professionals to support our expansion in the San Francisco Bay Area market and continued to add new core deposit accounts and relationships, as seen in the increase of non-wholesale deposits of 112 million in the three months ended March 31, 2024.

Despite continued external headwinds, we maintained our ability to conservatively underwrite, as evidenced by a 50 percent LTV on commercial real estate, manage expenses with our 45 percent efficiency ratio and deliver value to our shareholders with our \$0.20 per share dividends for the fourth quarter of 2023 and the first quarter of 2024.

The first quarter of 2024 exhibited continued margin compression, although swelling (sp) compared to prior quarters. We remained focused on the execution of our organic growth strategy and were able to maintain earnings and expense management trends during the quarter.

Loans have consistently grown since prior periods. The decrease in deposits and total (inaudible) during the quarter is the result of relying less on wholesale deposits and short-term borrowings, which positions us well for future growth.

Our pipeline continues to remain solid at the end of the first quarter of 2024 within verticals we have historically operated in as presented in the loan portfolio diversification slide.

Loans held for investment increased during the quarter by 22.4 million, 4.73 percent from the prior quarter, primarily within the consumer concentration of the loan portfolio.

Loan originations during the quarter were approximately 149.9 million while payoff and paydowns were 77.2 million and 50.3 million respectively.

Asset quality continues to remain strong. Though non-performing loans increased beginning in the third quarter of 2023, they continued to represent only .06 of the portfolio at the end of the first quarter.

At the end of the first quarter, the allowance for credit losses totaled 34.7 million. We recorded a .9 million provision for credit losses during the quarter, primarily related to the net effect of charge-offs, increases in qualitative reserves and reduction in reserves for qualitative factors.

The ratio of the allowance for credit losses to total loans held for investment was 1.12 percent at quarter end.

Loans designated as substandard totaled approximately 1.9 million at the end of the quarter, which was a decrease from the 2.0 million at the end of the previous quarter.

During the first quarter, deposits increased by 71.7 million or 2.35 percent as compared to the previous quarter. Non-interest-bearing deposits as a percentage of total deposits at the end of the first quarter increased slightly to 27.7 percent from 27.5 percent at the end of the previous quarter.

As noted earlier, we are pleased we had the net non-wholesale deposit inflows for the three months ended March 31, 2024. Our ability to grow deposit accounts supports our differentiated customer-centric model that our customers trust and value.

As seen through the mix of high dollar accounts and the duration of certain customer relations, we believe we have a reliable core deposit base.

To offer more detail on our deposit composition, I want to highlight that deposit relationships totaling at least 5 million constituted approximately 58 percent of total deposits. And the average age of these accounts was approximately nine years.

Local agency depositors accounted for approximately 24 percent of deposits as of March 31, 2024.

Overall, deposit balances have decreased when compared to the prior quarter as a result of our focus to rely less on costly wholesale deposits. Wholesale deposits, which we define as brokered deposits and public time deposits, decreased by 183.1 million. Non-wholesale deposits increased by 112 million, driven by a 125.7 million increase in interest bearing deposits, partially offset by a 13.7 million decrease in non-interest-bearing deposits. The cost of total deposits was 253 basis points during the fourth quarter.

We continue to be well capitalized with all capital ratios well above regulatory thresholds for the quarter. Our common equity tier one ratio increased from 9.07 percent to 9.13 percent between December 31, 2023, and March 31, 2024.

On April 19, we announced by a declaration by our board of directors a cash dividend of \$0.20 per share on the company's voting common stock, expected to be paid on May 13, 2024, to shareholders of record as of May 6, 2024.

On that note, I will hand it over to Heather to discuss the results of operations. Heather?

Heather Luck

Thank you, James, and hello, everyone. Net income for the quarter was 10.6 million. Return on average assets was 1.22 percent and return on average equity was 14.84 percent. Average loan yield for the quarter was 5.71 percent, representing an increase of seven basis points over the prior quarter.

Our net interest margin was 3.14 percent for the quarter while net interest margin for the prior quarter was 3.19 percent. Fed rate increases in 2023 continue to put pressure on deposit cost.

As a result of changes in interest rates and other factors, our other comprehensive loss was .7 million during the three months ended March 31, 2024, as (inaudible) net of tax effect increased on available for sell debt securities from 11.8 million as of December 31, 2023, to 12.4 million as of March 31, 2024.

Non-interest income decreased to 1.8 million in the first quarter from 1.9 million in the previous quarter, due primarily to reductions in gains from distributions on investments in venture backed funds and the recognition of rate lock and swap referral fees during the three months ended March 31, 2024. The decreases were partially offset by a reduction in net losses on the sale of securities, which did not occur in the first quarter of 2024.

Non-interest expenses grew by \$53,000 in the three months ended March 31, 2024, compared to the three months ended December 31, 2023. This is primarily due to an increase in salaries and employee benefits, partially offset by declines in advertising and promotional expenses as well as other operating expenses during the quarter.

Now that we've discussed the overall results of operations, I will now hand it back to James to provide some closing remarks.

James Beckwith

Thank you, Heather.

I want to thank everyone for joining us as we discuss the first quarter results. Five Star Bank has a reputation built on trust, speed to serve and certainty of execution, which support our clients'

success. Our financial performance is a result of the truly differentiated customer experience, which continues to power the demand for Five Star Bank's relationship-based services.

We attribute sustained success to our prudent business model and treating customers with an empathetic spirit, understanding and care. We are very proud to have earned the trust of those we serve, including our shareholders. As we lean into 2024, we are guided by a continued focus on shareholder value. As we monitor market conditions, we are confident in the company's resilience in any environment and remain focused on the future and our long-term strategy.

We will continue to execute on our organic growth and disciplined business practices, which we believe will benefit our customers, employees, community and shareholders.

We appreciate your time today. This concludes today's presentation. Now Heather and I will be happy to take any questions that you might have.

QUESTION AND ANSWER

Operator

We will now begin the question-and-answer session. To ask a question, those dialed in may press star, then one on your telephone keypad. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star, then two. Questions will be taken in the order received.

The first question today comes from Andrew Terrell with Stephens. Please go ahead.

Andrew Terrell

Hey, good afternoon.

James Beckwith

Hey, good afternoon, Andrew.

Heather Luck

Hey, Andrew.

Andrew Terrell

Just a couple around deposits for me - when did the runoff in the brokered deposits and then public fund time deposits occur during the quarter? And then do you have the weighted average cost of those deposits?

Heather Luck

So, going into the first quarter for the year, we have a weighted average rate of about 5.26 percent on the wholesale deposits, and that had a balance of about 360 million. We really did, I would say probably the second half of the quarter--

James Beckwith

--Yes--

Heather Luck

--The most -- most of the -- or the wholesale deposits ran off. So now, we're currently sitting at a weighted average rate of 5.12 percent.

Andrew Terrell

Okay--

Heather Luck

--And then total balance was 177 million.

Andrew Terrell

Yeah. And then can you talk about -- I mean, the remix this quarter was obviously very impressive. You've got sounds like 177 left of wholesale. Can you just remind us of the kind of deposit growth expectations for the year? And then would you expect any more runoff in the wholesale deposits within that kind of deposit guidance?

James Beckwith

Sure. We're going to shift through our 10 percent deposit growth. You know, we plan to end up in that -- you know, at 10 percent. You know, that includes accounting for runoff of -- you know, Q1 runoff of wholesale deposits.

I think as we sit right now, I wouldn't expect too great of a continued runoff of wholesale. Probably be pretty static, Andrew, for the rest of the year. But we'll look at this on a quarter-by-quarter basis. We kind of like where we are, and in a certain respect, maintaining relationships, particularly with the state of California, is important. You know, so I would think that -- we have a small, brokered piece left in July.

Heather Luck

42 million.

James Beckwith

42 million, which, hopefully, we'll be able to eliminate that, but nothing probably greater than that, Andrew.

Andrew Terrell

Okay. Great. I appreciate it. And then could you maybe just compare, contrast for the -- the non-wholesale deposit growth, I think it was 112 million or so this quarter, just the weighted average cost you're bringing, kind of new money on the balance sheet today versus what we saw roll off in the first quarter?

James Beckwith

Sure. A lot of the balances that we're bringing on right now are interest bearing, and when I think about -- you probably looked at how -- what we expect in terms of non-interest bearing and interest bearing, you know, that weighted average rate is probably around -- a little shy of 3 percent. But the interest bearing stuff is -- probably has about a 4 percent handle on it, as I'm thinking all this through. And so, if we're successful in our -- you know, for the remainder of the year with non-interest-bearing deposit increases, and that's really driven by new relationships that we're bringing on, you know, that'll work those numbers down.

I think our San Francisco effort in terms of yield that we're paying those deposit customers -- Heather, do you have that information? I'm trying to recall it off the top of my head.

Heather Luck

(Inaudible) quotes at 3.

James Beckwith

Yeah, it's a little shy of 3 percent.

Heather Luck

Yeah.

James Beckwith

(Inaudible) I think that was in (inaudible) deck.

Heather Luck

Correct.

James Beckwith

So, that's kind of what we're looking at right now in terms of what we're bringing on these new relationships -- these new relationships on.

And, Andrew, it's important to know that we -- you know, as we bank these new customers, and -- you know, across our entire footprint, you know, we're really after their operating accounts and their liquidity. So, we look at things in totality in terms of cost for funds. So, if we can pay somebody 4 percent for their liquidity and just bank their non -- their transactional account, if you will, you know, that -- we think that that's a winning strategy, and hopefully, we can deliver the entire relationship sub 3 percent.

Andrew Terrell

Yeah, totally appreciate that. Understood. If I could ask just one last one, Heather, around the margin - do you have the margin in the month of March?

Heather Luck

Oh, in the month of March? I do. So, our net interest margin for -- just let me pull up that piece of it. Net interest margin just for the month of March was about 3.18.

Andrew Terrell

Perfect. Okay, thank you for taking the questions. I'll step back.

Heather Luck

Thank you.

Operator

Again, if you have a question, please press star, then one.

The next question comes from Gary Tenner with DA Davidson. Please go ahead.

Gary Tenner

Thanks. Good morning. I wanted to ask, on the expense side, you know, what the near-term thinking is on expense levels kind of fully loaded for, you know, new hires?

Heather Luck

Yeah. So, I think if we look at, for Q2, I think that they add about \$500,000 for Q2's expenses to what we incurred for Q1. That should put your model in good shape there. We do have some new

hires, but then also some expenses for conferences that we have run into that are a little bigger than Q1.

James Beckwith

And our advertising spend is gonna go up in the second quarter, third quarter, and fourth quarter as we continue to develop the Bay Area.

Gary Tenner

Okay, appreciate it. And then I may have (inaudible). I heard you mention I think the March NIM (sp), Heather, but did you provide the spot rates as of March 31? If you did, I apologize for missing it.

Heather Luck

Oh, no, sure. The spot rate for cost of deposits was 249.

Gary Tenner

Great. Thanks very much.

Heather Luck

Uh-huh.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to management for any closing remarks.

James Beckwith

Great, thank you. Five Star Bancorp is on a continued path of growth as we execute on strategic initiatives, which include growing our verticals and geographies while attracting and retaining talent. Our people, technology, operating efficiencies, conservative underwriting practices and expense management have also contributed to the success we share with our shareholders and employees.

These successes include numerous rating and awards. In the first quarter, the company's leadership was recognized by the Sacramento Business Journal, on the Power 100 List and the Women Who Mean Business List. Company leadership also received the National Association of Women Business Owners Outstanding Women Leaders Executive Woman Award.

Also in the first quarter, two of our customers were recognized by the Sacramento Small Business Administration in the categories of Family Owned Small Business of the Year and Minority Small Business Champion.

Five Star Bank continues to be a driving force for economic development, a trust resource for our customers and a committed advocate for our community.

We look forward to speaking with you again in July to discuss earnings for the second quarter of 2024. Have a great day and thank you for listening.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.