Conference Call
Financial Results

Third Quarter 2021

September 1, 2021

LAURENTIAN BANK
FINANCIAL GROUP

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Operator

Welcome to the Laurentian Bank Financial Group conference call. Please note that this call is being recorded. I would now like to turn the meeting over to Susan Cohen. Please go ahead, Ms. Cohen.

Susan Cohen, Director, Investor Relations

Bonjour à tous. Good morning and thank you for joining us.

Today's opening remarks will be delivered by Rania Llewellyn, President and CEO, and the review of our third quarter of 2021 financial results will be presented by Yvan Deschamps, Executive Vice President and Chief Financial Officer, after which we will invite questions from the phone. Also joining us for the question period are several members of the Bank's Executive Leadership Team: Liam Mason, Chief Risk Officer; Kelsey Gunderson, Head of Capital Markets; Éric Provost, Head of Commercial Banking; and Karine Abgrall-Teslyk, Head of Personal Banking.

All documents pertaining to the quarter can be found on our website in the Investor Center.

I would like to remind you that during this conference call, forward-looking statements may be made, and it is possible that actual results may differ materially from those projected in such statements. For the complete cautionary note regarding forward-looking statements, please refer to our press release or to Slide 2 of the presentation.

It is now my pleasure to turn the call over to Rania Llewellyn.

Rania Llewellyn, President and Chief Executive Officer

Thanks Susan.

Bonjour à tous. Good morning from Montreal and thank you for joining us today.

As summer comes to a close, I hope that everyone had an opportunity to disconnect and recharge, particularly this year, as the impact of COVID continues to take its toll on everyone's physical and mental health. To support our employees, I encouraged everyone to take their vacation days and as a Bank, we provided an additional four paid Friday afternoons off this summer.

Over the past few months, we have been working to refine our future of work plans. We conducted a company-wide survey to hear directly from our employees on their work habits, expectations, and preferences. One thing we've learned is that a one-size-fits-all strategy is not realistic, and that we must adapt to new ways of working. That's why we will be pursuing an employee-centric strategy and adopting a Hybrid Model, where working from home is our first approach for all tasks that can be performed remotely.

We will also not begin any mass return to head office and corporate office premises until at least January 2022.

We are closely monitoring the impact of the delta variant on the economy, particularly labour market conditions, as Canada plans to phase out government income support programs this fall. We expect that interest rates will remain low and spending intentions of both consumers and businesses should create a favorable backdrop for loan growth.

Turning now to our results, the momentum that we have been building over the first half of the year continued into the third quarter – delivering adjusted net income of $59.0 million. This represents an increase of 4% quarter-over-quarter and 25% year-over-year with adjusted earnings per share of $1.25.

Our results were driven primarily by strong performance in Real Estate Financing, lower provision for credit losses and our continued focus on cost discipline. The PCL includes releases of allowances on performing loans of $3.6 million reflecting improvements in economic conditions.

I am also pleased with another solid quarter from Capital Markets. Growing fee-based revenues from the Equity and advisory group helped produce our second highest quarter on record for this business.

The bank also continues to maintain healthy liquidity levels and a strong capital position with a CET 1 ratio of 10.3%, up 20 bps quarter-over-quarter and 90 bps year-over-year.

In the third quarter, inventory financing was impacted by continuing supply-chain disruptions and high consumer demand for recreational vehicles which resulted in the lowest dealer credit utilization rate on record of 28%. We expect that supply chain disruptions and high consumer demand will continue to remain a challenge for most of 2022. To counter these impacts and to position us well for the post-pandemic recovery, our business development team has expanded the dealer network by more than 20%. When credit utilization rates rebound, every incremental one percentage point of utilization results in $50 million of assets and a return to pre-pandemic utilization levels in the mid-fifties would generate over one billion dollars in additional assets.

This quarter also saw some key developments that I would like to highlight:

- The Bank purchased group annuity contracts to de-risk our pension plans which reduces our non-operating financial risk and administrative costs. The transaction resulted in a net after-tax settlement gain of $5.2 million which is excluded from adjusted earnings.

- The Real Estate Finance Group had very strong performance with growth of 6% quarter over quarter and 18% year over year. The pipeline is at an-all time high level of $4 billion which is expected to fuel future growth and profitability.

While I am pleased with our overall performance for the first three quarters of the year, we do not expect it to be a straight-line to success.

You will recall from previous quarters that we have established three strategic pillars that are guiding all our efforts and actions. They are:

1. Cultivating a “Customer First” culture;
2. Driving an “Agile and Innovative Mindset”; and,
3. Engaging and Empowering our employees to work as “One Team”.

From those pillars, we identified three key priorities for 2021:

1. Renew the senior leadership team and organizational structure;
2. Increase our efforts on cost discipline while pivoting to structural cost opportunities; and,
3. Conduct a thorough review of the Bank’s operations and develop a new strategic plan.

We have made significant progress on all three of these priorities and I would like to provide a brief update on each one.

First, following up from last quarter where we announced a search for a Chief Technology Officer, I am pleased to announce that Beel Yaqub joined Laurentian Bank as the new Executive Vice President and Chief Information Technology Officer in July. He brings over 20 years of experience in digital technology, business transformation and data insights to the Bank and we are extremely pleased to have him on the team.

Second, as I have said before, a key focus area for the Bank this year is in managing our costs. While we continue to pivot towards identifying large cost optimization opportunities, we are finding low-hanging fruit and executing against those initiatives. A few examples include:

- Consolidating vendor agreements to bring more value for the Bank, including an instance where the Bank entered into seven agreements with the same partner;
- Simplifying our Visa product offering from eight to four, to enhance the customer experience while reducing costs; and,
- Conducting a strategic sourcing exercise to consolidate our printing service contracts resulting in cost savings for the Bank.

I am a big believer in every penny count. We are looking at all opportunities that contribute to our cost savings and this work is starting to be reflected in our results, with our adjusted efficiency ratio improving by 150 basis points quarter-over-quarter to 68.4%.

Third, as you know, we are continuing to conduct a thorough review of the Bank's operations. Over the past two quarters we identified shortfalls in our mortgage business including a complex customer experience, lengthy processes and inconsistent service levels.

To improve the customer experience, we are ensuring we have the right people, processes and technology in place. Initiatives this quarter include:

1. First, the creation of a new Residential Real Estate Secured Lending business unit within Personal Banking. This new unit will allow for greater accountability and cross-functional collaboration in delivering a seamless experience for our customers and renewing growth;
2. Second, the implementation of "DocuSign", a digital tool for ease, convenience and collection of customer signatures; and,
3. Third, the integration of technology like an Automated Valuation Management system which enables the Bank to save processing time in valuing properties from days to seconds and saves customers hundreds of dollars per transaction.

While we know that this is a multi-year journey to improve the customer experience and to renew growth, we do expect to reap benefits along the way.

Last quarter, we committed to completing a strategic review of our digital roadmap and to sharing our progress. As a result of our review, we have identified three key areas of focus:

1. First, we will work to close foundational gaps in our offering. For instance, we currently have two different experiences for our retail customers depending on which platforms their accounts reside on. We will streamline this process and provide new digital offerings such as a mobile app and tap-enabled debit cards for all customers;
2. Second, we will enhance our digital onboarding, sales, and servicing capabilities to allow us to expand our reach to new customers and deepen relationships with existing customers; and,

3. Third, we will simplify our offering and improve the end-to-end digital customer experience.

Similar to our mortgage review, we are ensuring that we have the right people, processes and technology in place. We will come back in future quarters with further updates.

As you know, the Bank's ESG journey remains a key priority. To further support our efforts of making Laurentian Bank a place where people, businesses and communities thrive, I'm pleased to share some key developments over this past quarter:

- We launched our PRIDE employee resource group and Courageous Conversation Series for LGBTQ2S+ community and allies;
- We rolled out a mandatory Unconscious Bias training program for all employees;
- We initiated an RFP to conduct a Climate Risk Assessment for the whole Bank to better understand our impact on the environment and areas of opportunity; and,
- We continue to be an active participant in Green bond issuances.

As we head into the Fall, we will continue to work with our employees to ensure their safety and that of our customers remains our top priority.

We will also look for opportunities to generate new business and grow revenues as the economy reopens while maintaining our disciplined management of expenses.

I am now pleased to turn the call over to Yvan.

Yvan Deschamps, Executive Vice President, Chief Financial Officer

Merci, Rania.

Bonjour à tous, and good morning everyone.

I would like to begin by turning to slide 10 which highlights the Bank's financial performance.

For the third quarter of 2021 adjusted net income and EPS reached $59.0 million and $1.25 respectively. Materially lower provision for credit losses contributed to adjusted net income improving by 25% compared to a year ago. Total revenue grew by 3%. An improvement in economic activity contributed to an increase in lending fees and continued good performance in financial markets drove an increase in market-related revenues. Adjusted non-interest expenses increased by 3% due to higher performance-based compensation. This resulted in adjusted pre-tax, pre-provision income, or PTPP, growing by 1% year-over-year.

Reported net income and EPS in the third quarter were $62.1 million and $1.32 respectively and were higher than adjusted results. The variance with adjusted results is partly explained by the Bank's purchase of group annuities to de-risk its pension plans. Specifically, the Bank purchased $346 million of group annuity contracts from a Canadian insurer and transferred $353 million in obligations. This transaction strengthens the balance sheet, lowers the risk from pension obligations, reduces administrative costs and further simplifies operations. It also resulted in the recognition of a net settlement gain of $7.1 million or $5.2 million on reported net income in the third quarter of 2021 and is included in the reported results adjusting items.

I would now like to review the drivers of our performance that begin on slide 11. Year-over-year, net interest income and net interest margin were relatively unchanged as improved funding costs were largely offset by lower average loan volumes.

Turning to slide 12, other income was up 7% from a year ago. The increase was due to higher lending fees stemming from an improvement in economic activity and commissions from the sales of mutual funds. Compared to the second quarter, the 2% increase was driven by the strong performance in real estate lending.

Slide 13 highlights that adjusted non-interest expenses were up $5.2 million or 3% compared to last year. Salaries and benefits increased by $4.5 million on an adjusted basis, due to performance-based compensation as the Bank delivered stronger results. The adjusted efficiency ratio of 68.4% was 30 basis points higher than a year ago and improved by 150 basis points compared to last quarter as a result of higher revenues.

Slide 14 presents our sources of funding which we continue to strengthen, diversify and optimize.

- First, the Bank increased its use of securitization over the past year by $1.4B. Considering this increase and loan volumes, we chose to reduce term deposits from Advisors and Brokers by an equivalent amount. These decisions optimize our funding costs and provide greater flexibility as growth resumes.
- Second, personal branch notice and demand deposits increased year-over-year by $200 million or 7%.
- Third, we issued $250 million of covered bonds which is the most efficient form of funding conventional residential mortgages that will allow the Bank to deliver competitively priced products to our customers. The covered bonds were classified as wholesale deposits.
- Finally, the Bank issued $125 million of Limited Recourse Capital Notes with the proceeds used to redeem the Preferred Share Series 15.

Slide 15 highlights our strong capital position. The CET1 capital ratio, presented under the Standardized approach, stood at 10.3%. This was an increase of 20 basis points sequentially and 90 basis points year over year and was mainly driven by internal generation of capital.

Slide 16 highlights the commercial loan portfolio which grew by 2% sequentially. Growth in real estate lending of approximately $500 million, was mostly offset by a decrease in inventory financing of about $300 million. The soaring prices of single-family homes has created strong demand for multi-residential and condo projects, fuelling the pipeline of our construction lending group. We continue to maintain disciplined underwriting standards as evidenced by the LTV on the term loan portfolio of 57% and the LTV on the uninsured multi-residential mortgage portfolio of 55%. Overall, the strength of our underwriting, good diversification and strong collateral, contribute to the high quality of the commercial loan portfolio.

Slide 17 presents the pan-Canadian residential mortgage loan portfolio. Residential mortgage loans slightly declined by 1% during the quarter. As Rania mentioned, we are taking actions to review our mortgage processes to improve the customer experience and to renew growth. Although improving the performance of the mortgage business will be a multi-year journey, we expect to gradually reap benefits along the way.

The Bank's residential mortgage portfolio remains relatively weighted towards insured mortgages when compared to the industry at 56%, and combined with a low LTV on the uninsured portfolio, contributes to reducing the overall risk of this business.

Turning to Slide 18, allowances for credit losses totaled $183.3 million. The sequential decrease of $2.2 million includes $3.6 million of releases of allowances on performing loans reflecting an improved economic outlook. ACL continues to take into consideration our cautious approach given the uncertainty related to new variants, as well as the winding down of government support programs. To date, we have released about half of the pandemic related build up of reserves and may release more over the coming quarters should macroeconomic conditions continue to improve. Scenario weights remain unchanged.

As shown on slide 19, the provision for credit losses was $5.4 million in the third quarter of 2021. Compared to last quarter, PCL increased by $3.0 million, due to lower releases of provisions on performing loans and was partially offset by lower provisions on impaired loans. The PCL loan ratio stood at 7 basis points in the quarter compared to 3 basis points last quarter.

Gross impaired loans, on slide 20, increased by $10.6 million from last quarter, mainly reflecting an increase in commercial impaired loans which relate to a few loans with no industry concentration. We remain adequately provisioned.

I would like to offer some thoughts on how we see the fourth quarter developing.

- Net interest income and Net Interest Margin are expected to be relatively in line with Q3.
- We continue to expect good performance in Capital Markets although financial markets may gradually normalize.
- The Commercial Banking pipeline is strong, particularly in real estate lending. However, loan growth is expected to be impacted by the lingering softness in inventory financing. As previously mentioned, we now expect that supply chain disruptions and high consumer demand will continue to remain a challenge for most of 2022 based on feedback received from our customers and industry participants. In the interim, we continue to expand the dealer network, positioning us well for the anticipated recovery.
- We will continue our focus on cost discipline and aim to keep the efficiency ratio below 70% for the remainder of 2021.
- Provision for credit losses continues to be difficult to predict. The surge in the Delta variant is adding to economic uncertainty, even though economic indicators have been moving in the right direction. Consequently, we will remain prudent in managing ACL in the coming quarters but could see further releases should the economic recovery continue.

Considering these factors, we expect PTPP for the fourth quarter to be relatively in line with the third quarter.

I will now turn the call back to Susan.

Susan Cohen, Director, Investor Relations

Thank you. At this point, I would like to turn the call over to the conference call operator for the question-and-answer period. Valerie, please proceed.

Operator

Thank you. If you would like to ask a question, please signal by pressing star one on your telephone keypad. If you're using a speakerphone, please make sure that your mute function is turned off to allow your signal to reach our equipment. Again, press star one, to ask a question. For participants wishing to ask a question, please remember to mute yourself once you complete the question to negate any background noise while the presenters are responding. If you have a follow-up to the response, please then unmute yourself to respond. Thank you. We'll pause for just a moment to allow everyone an opportunity to signal for questions. We'll take our first question from Meny Grauman of Scotiabank, please go ahead.

Meny Grauman, Scotia Global Banking and Market

Hi, good morning. You've talked over the past few quarters about a number of changes you're making in the residential mortgage business and I'm wondering, when do you expect to see growth in balances on a sequential basis? Is it clear to you when you're going to see that? What's your expectation from your team in terms of that specific indicator?

Rania Llewellyn, President and Chief Executive Officer

Thanks, Meny for the questions. So over the last couple of quarters, we've really been focusing on completing a thorough end-to-end process review of all aspects of mortgages, whether it be origination or retention, both in our B2B distribution network, as well as in our branches. And obviously, that's uncovered that we really have a highly complex customer experience as well as a lengthy process and inconsistent customer service. We had highlighted in the last quarter that we've launched a couple of key pilots. One of them was segmentation of our mortgage brokers where we assigned one individual contact to follow the file from an end-to-end perspective. And it's early days, it's a small pilot, what we've seen is that it did improve our funding ratio and it did increase the origination volumes.

Recently in this past quarter, we also introduced a new pilot focused on retention. So, we've created a centralized retention team, and that's really to proactively reach out to those customers who their mortgages are up for renewal well before then, so that we can proactively manage that. And as I said in my opening remarks, we've introduced a number of other things where it's the new unit, and that's really to bring in focus and accountability under one leader who has a deep understanding of mortgages. And will be responsible and accountable for the growth of that business, as well as improving the customer experience, and introduced a couple of new digital tools to improve the customer experience as well as speed up the process.

Meny, you and everybody on this call would appreciate mortgages, it's a multi-year journey. It's going to take a lot of hard work. It's not rocket science; it's making lots of little fixes while we're looking at technology solutions and partnership opportunities for us to speed up the process. But at this point, I would say it's a multi-year journey, 18 to 24 months. It's going to take around 18 to 24 months to really start seeing some benefits, but we're hoping to reap some benefits along the way as we introduce some more changes.

Meny Grauman, Scotia Global Banking and Market

Thanks for that. And maybe just as a follow-up, from the outside looking in, how should we measure success here as time goes on. Maybe if it's not balances, are there other indicators that are going to be important to track? Are you thinking about providing additional disclosure to that point?

Rania Llewellyn, President and Chief Executive Officer

So I would say Meny, if we look at 2021, the theme of this year has really been a theme of resetting and rebuilding. And so, our focus has been renewing our senior leadership team, which we've had significant progress, and Beel was the latest addition to our leadership team. And really focusing on ensuring that we have the right strategy to enable sustainable profitable growth. And that's something that we'll share in due course. For next year, given some of the macroeconomic concerns that we have - softness that we're looking at from a supply chain disruption perspective and the Delta variant. So, there's a lot of macroeconomic conditions that are beyond our control. I would say 2022 is really going to be year of mobilization and execution. So, we'll have a strategic roadmap, we'll have the right team, and now we need to start executing, and that'll take time.

I would say the commercial bank is well-positioned particularly in our real estate lending portfolio. We're also going to see growth in our equipment financing business. But again, the biggest headwind there is our inventory financing. I mean, it's a high-margin business in the mid-digits - mid-single-digits that generate some revenue. And so, we're really at the mercy of the supply chain disruptions coming back, loosening up. And then on the personal side, as I mentioned in responding to your previous question, it is going to be a longer road to recovery. So, we're going to continue to focus on cost optimization, while we're building the right platforms for our future growth. I mean, the other thing too is, we don't have a mobile app at Laurentian Bank. We don't have tap on our debit cards. So those are things that we are working on, which will also generate growth opportunities once we launch them in the market to attract new customers, new business, then we can cross sell them on all of our products and services.

Meny Grauman, Scotia Global Banking and Market

And then you touched on the commercial loan portfolio, definitely looks like it's the real estate side of that that is really driving the growth that we're seeing. You talked about supply shortages. But I guess when you look at the numbers and even digging deeper, what gives you confidence that it's really about the supply side that there's nothing more fundamental here in terms of maybe more of the - the non-real estate side of the commercial lending. What gives you confidence that you're on track there and there's no other sources of weakness besides supply side issues that you highlighted?

Rania Llewellyn, President and Chief Executive Officer

So, Meny, we have three key specializations that are within our commercial book of business inventory financing, real estate financing, and equipment financing. And so, like you said, inventory financing is the one that's really impacted by the supply chain disruptions. As I mentioned, every 1% increase in utilization is an additional $50 million in assets. So, if we were to return to pre-pandemic levels, which is mid-50s in utilization, and currently we're sitting at a record low of 28%, that's an additional billion dollars in assets. So that's inventory financing. And we're not standing still, our business development salespeople are out there and they're bringing in some more business. We've increased our network of dealers by 20% year-over-year. So, that's really one aspect.

Real estate financing was up 6% quarter-over-quarter, 18% year-over-year. And we're optimistic in terms of that business because we have a strong pipeline of projects in our pipeline of $4 billion. And that's a 10% to 15% increase. It's higher than our 2020 and 2019 average. So, we're quite confident there that the growth trajectory will continue there. And I would say on the equipment financing, again, there are macroeconomic conditions, and it is also impacted in certain respects by supply chain, but not as much as inventory financing. So, we will see some growth. So, I would say 2022, we'll see some growth, but really the big growth is going to come probably in the years to come once the macroeconomic conditions return to normal.

Meny Grauman, Scotia Global Banking and Market

Thanks so much.

Operator

Thank you. If you find that your question has been answered, you may remove yourself from the queue by pressing star two. We'll take our next question from the line of Paul Holden of CIBC. Please, go ahead.

Paul Holden, CIBC

Thank you. Good morning. I have a few questions for you related to the digital journey you're going through. And I guess the first question I have is just noticed looking at technology costs down a little bit on a year-to-date basis. So just wondering, one, is why is that a number that's showing a year-over-year decrease, and maybe there's some efficiencies or vendor consolidation that's benefited that line. And then two, should we expect to see a higher growth in that line in 2022?

Rania Llewellyn, President and Chief Executive Officer

So that's great. Thanks for the question, Paul. So maybe I'll start with kind of the digital journey, what we've uncovered, and then I'll move into technology and how technology will be enabler for us for growth and why you're seeing a little bit of a drop. So, let me start there, and if any of my colleagues want to jump in, they can. I would say in terms of the digital journey we've identified some key foundational gaps. And like I said, it may be a surprise to everyone on the call, but we don't have a mobile app, and we're hard at work in terms of delivering that to the market. We don't have tap on debit, which is obviously restrictive, particularly during a pandemic.

We have two platforms which gives you two different experiences. And so, I would say if there's one theme that is a guiding principle for everything that we'll be doing at Laurentian Bank is simplification. We need to simplify our platforms; our technology platforms are complex. So, there's an opportunity for us to simplify as we modernize. And so, we're reviewing all aspects of the technology to ensure that we're spending money where we need to, to enable and drive sustainable profitable growth. So, there are two levers, it's either sustainable revenue growth, or if there are opportunities for cost efficiencies.

With Beel joining the team now, there's an opportunity for us to continue to review all aspects and all technology projects, but it's also part of a bigger cost optimization initiative. As I said in our opening remarks, we had lots of agreements with different vendors, so there's lots of opportunities, low hanging fruit for us to simplify, as well as generate some cost efficiencies as we go along. However, we will need to invest in technology. We just need to be more strategic to ensure we're investing in the places that are going to help us drive revenue, as well as find savings, and improve the customer experience.

Paul Holden, CIBC

Got it. Okay. And then, hearing the comments you've made on sort of some gaps in the product offering and customer experience, like how should I look at the trend in digital deposits? Because that's clearly not where you wanted to be again with year-over-year deterioration and quarter-to- quarter deterioration on digital deposits.

Rania Llewellyn, President and Chief Executive Officer

So, Paul, that's why mobile is absolutely crucial. Once we have a mobile app, it'll definitely help and assist in terms of attracting net new deposits while returning - retaining existing deposits. The other thing too is enhancing our digital onboarding. It's a very complex digital experience right now to get onboarded, to open a bank account. So those two things combined will be absolutely critical for us to bring in some more deposits. The other thing too that we're working on is a cash management digital solution for the commercial bank because we don't have one right now either. That's something that we're looking - working hard in terms of scoping it to launch it. So I would say those two critical components. But just to keep in mind, when we're managing deposits, we're proactively managing the amount of deposits that we have in the bank relative to the growth in our assets. So that is a deliberate move that we have as well, and then making sure that we're optimizing our source of funding.

Paul Holden, CIBC

Got it. And as I think about that equation sort of longer-term, how should I think about the relative cost of those digital deposits? Because I would have thought of those as being margin-enhancing over time. Am I correct in that assumption?

Rania Llewellyn, President and Chief Executive Officer

So I would say, it really depends on the customer base it's going to attract, what the product offering is, and that's going to be directly connected to the margin and the value proposition that we're offering. I think that in a mobile world you're going to be attracting all kinds of customers. And you can leverage the platform to offer different deposit offers or is it for your core customer base that you're cross selling. But it'll definitely be a customer acquisition play for us which will ultimately drive deposits as well as cross sell opportunities for other products that we have.

Paul Holden, CIBC

Okay. And final question I have on this topic is related to open banking. I mean, you're aware, and probably everyone is aware on this call that the federal government wants to push through open banking starting 2023. Not that far down the road. I was just wondering how you're thinking about that maybe - and maybe it's too early in your process in terms of the digital review, but just thinking about the opportunity broadly in terms of open banking and how that may benefit Laurentian.

Rania Llewellyn, President and Chief Executive Officer

Yeah. So, what I would say, Paul, is I think open banking is an opportunity for all service providers particularly in the financial industry space to enhance the value that we can deliver to our customers. So I think it's an opportunity that we can sharpen our value proposition to our customers. Work with other partners to help in terms of delivering even additional services beyond financial services. I think the most important thing that all banks are thinking of, including Laurentian Bank is how do we protect the customer information and data. That is going to be absolutely paramount as we move forward with open banking. So it's definitely something that is going to be embedded in our strategic roadmap, whether it be from a product design, technology, partnership strategy, and so on. So, I truly believe it's an opportunity and enhance the value proposition, and help us differentiate our offering in the market.

Paul Holden, CIBC

Got it. Okay. And one last small one from me, just on the lending fees, I mean, it was abnormally high this quarter and that was attributed to real estate lending volumes, so appreciate the explanation. But just trying to think about where it came in this quarter versus typical run rate, like if we assume that CRE remains strong, should we assume similar fees going forward or is there anything abnormal in this quarter?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

This is Yvan. I'll take that one. The lending fees are pretty good and strong this quarter, and that definitely came from the performance in real estate. So, the level that you should assume in terms of run rate, it'd be a good guess to look at the average year the last few quarters that we have. So, it may be a bit lower than what we had in Q3, but based on the pipeline and what we expect from real estate, should be a good level going forward.

Paul Holden, CIBC

Thank you. That's helpful. And that's it from me.

Operator

Thank you. We'll now take our next question from Lemar Persaud of Cormark Securities. Please go ahead.

Lemar Persaud, Cormark Securities

I want to start off by turning back to the residential mortgage business. I'm just wondering if there's anything you saw, Rania, through the course of your review this quarter that caused you to push out the timing of the recovery in that business. I seem to recall 12 to 18 months last quarter being the timing of the mortgage review, and then I think I heard you mention it was going to be 18 to 24. Is am I just reading too far deep - too deep into your comments or is there something that you uncovered there?

Rania Llewellyn, President and Chief Executive Officer

So, Lemar, I think there are two different comments. One is how long it's going to take us to actually review the entire business and come up with a strategic plan. And that's why we said it's going to take almost 12 months to just figure out and come with kind of the details of that. But we've always said, anyone who's run the mortgage business, it's going to take time for that ship to turn around. It's not a start-up business, it's complex, it's highly regulated, and so there's lots and lots of moving parts. We have different distribution channels. We've already, like I said, started seeing some improvements in a very minor way. But it's going to take 18 to 24 months for us to really start seeing the impact of our efforts. So, it's not like we're standing still, we're making the changes but it's part of our broader strategic review.

Lemar Persaud, Cormark Securities

Okay. So, there was nothing then that caused you to push out the timing throughout the course of Q3, that you uncovered?

Rania Llewellyn, President and Chief Executive Officer

No, no, Lemar. No, no. I think we very quickly highlighted to you our processes are complex and we had mapped out last quarter just the origination journey and now we've expanded it to the retention journey. And last quarter it was focused on the advisors. We mapped out just the advisor business, so the B2B business, and now we've expanded it to include the branches. And I would say that it's quite consistent. The issue is we have different journeys for the B2B business versus branches. So, we really need to simplify. Creating that new unit will bring that focus and will help us come up with one journey for each of the applications. And in that way, it'll just make it easier for us to figure out what is it that we need to offer to automate, what do we need to digitize? How can we improve things? And so, stay tuned on how we're going to move forward going forward.

Lemar Persaud, Cormark Securities

Okay, thanks. So, thanks for that. That's helpful. And then maybe just flipping back to digital and just going to the digital deposits, would it be fair to suggest that the digital deposits are going to coincide with the introduction of the mobile banking app? So maybe my question then blows now to, when do you see the introduction of the mobile banking app?

Rania Llewellyn, President and Chief Executive Officer

So, we're hoping to introduce the mobile banking app by the end of the calendar year. But we're building it in agile. So, it's going to have - so you're going to launch your first minimal viable product, which will have certain foundational elements. It's not going to have all of the functionality that we need. And so, it's going to be a continuous release of different functionality that's going to happen over the next 12 months. And it's not one of those things where you just kind of turn it on and the deposits start coming in. So, it'll obviously have to be supported by a proactive sales campaign, product offering, so it's going to take some time. But yes, we are very excited in terms of closing that gap, because that will be a key enabler for us to attract deposits as well as new customers to the bank.

Lemar Persaud, Cormark Securities

Great. Thanks. That's it from me.

Operator

Thank you. And we'll move to our next question from the line of Sohrab Movahedi of BMO Capital Markets. Please go ahead.

Sohrab Movahedi, BMO Capital Markets

Thank you. I just wanted to clarify one question and - one answer and get to a couple of other questions in. I think you mentioned, Rania that if the utilization rates, I think on the commercial products were back at pre-pandemic levels that would be the equivalent of about a billion dollars in additional assets. Would that also be about the same amount of incremental RWA on the balance sheet at those utilization rates?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

I would say it's not exact, Sohrab, but it's pretty close to assume it's roughly in line. Yes.

Rania Llewellyn, President and Chief Executive Officer

And, Sohrab, just to be clear, that's just the inventory financing. So, it's not the big commercial real estate loans. It is inventory financing within commercial.

Sohrab Movahedi, BMO Capital Markets

Okay. Thank you. And so then secondly, when you're looking at the residential real estate review, I think that you've kind of articulated over the last number of quarters, is it only a process improvement review or do you anticipate that one of the outcomes could be that their composition or the risk texture of that portfolio may change between, I don't know, insured and uninsured or origination LTVs or something like that? Is it possible that your risk appetite may also morph as you improve on the processes there?

Liam Mason, Executive Vice President, Chief Risk Officer

Sohrad, it's Liam. Thank you for the question. Right now, we're very happy with our risk appetite in the mortgage review. Indeed, our product offering was recently recognized with an award. We operate both in the prime and the insured spaces, and clients seem to like our broad offering. We don't have any change in our risk appetite. That said, we have a very high proportion of our mortgage portfolio insured as Yvan mentioned, and we have a relatively low LTV. So that will ebb and flow as we build the business.

Rania Llewellyn, President and Chief Executive Officer

And so, I would add to that, Sohrab, is we're obviously going to be looking at all aspects in terms of the sales process our product construct, our end-to-end process, how we're interacting with the customer, our back-end processes. Can we actually make it a lot more efficient by partnering up with somebody else? You know, how can we make the experience a little bit more enhanced? So, we're looking at all those aspects, but from a risk perspective, we're quite comfortable with our current risk appetite and we're not anticipating any changes at this point.

Sohrab Movahedi, BMO Capital Markets

Okay. That's perfect. And then the last one, I think we've talked a little bit about the core banking system and some work that maybe has been put on hold and a more strategic review over there. I mean, as you think about your digital deposit capture and some of those technology type projects here, how dependent is that on having resolution, if you will, on what's happening with the core banking system?

Rania Llewellyn, President and Chief Executive Officer

What I'd say is a lot of the customer facing technology can be quite separated from the back-end systems, but we are looking at things holistically. And so with Beel coming in right now, and we're in the midst of our strategic review, and so he will be coming up with a technology architectural roadmap of how can we best deliver that in the timeframe that we need to generate growth while modernizing and building for the future. He's coming at an opportune time so stay tuned for more on that.

Sohrab Movahedi, BMO Capital Markets

Okay. Thank you very much.

Operator

Thank you. I will move to our next question from the line of Darko Mihelic of RBC Capital Markets. Please, go ahead.

Darko Mihelic, RBC Capital Markets

Hi, thank you. Good morning. Just first a very high-level question for Rania, I think. I appreciate this is difficult, right? I mean, every quarter we're pestering you for more information on your strategic view and so on. Is there going to be a big reveal of this strategic review and when is that? I'm just trying to piece together every quarter of what we're building on here with respect to the outcome of the strategic review. Is it next quarter? Is there something sort of lined up?

Rania Llewellyn, President and Chief Executive Officer

So Darko yeah, I know it's a little frustrating and I kind of feel sometimes like I'm a broken record, but we are going to be hosting an investor day in early 2022. We haven't set the date yet. It's part of my closing remarks. But Yvan and I are hoping that we can provide some form of guidance at a very high level in Q4, but stay tuned for more on that, Darko.

Darko Mihelic, RBC Capital Markets

Okay. I just wanted to make sure I had something as we sort of go. The next couple of questions are related to your position - your capital position and the upcoming potential removal of restrictions from the regulator, whenever that may be. Your capital position is relatively strong, your stock trades well below book value. One of your peers is now adopted like an ATM. And so the question sort of naturally, certainly that evokes is, in the event that the regulator does lift the restriction on capital return, would you consider doing something similar, ripping down the ratio, buying back a lot of stock, which makes a ton of sense for shareholders, and then potentially engaging in ATM should growth reappear in a much stronger than anticipated fashion, or do you see yourself running a bit differently with a bigger cushion to the minimum capital ratio?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

Thank you for the question, Darko. This is Yvan. So, as you mentioned, very pleased with the capital level that stands at 10.3, an increase quarter-over-quarter and year-over-year. And the good news is that it came from internal generation of capital, which is a good sign. But our first objective remains to grow the asset base. So that's definitely where we intend to use the capital. So, at this point, we don't intend to use an ATM. We definitely are focused on growing this business and we're taking actions like we mentioned on mortgages and other products as well. So, stay tuned for the end of the year when we unveil the strategic plan. We'll give you more guidance on this. And as you know, all of that is prevented at this point. So, we also need to wait for OSFI before providing any more guidance on it.

Rania Llewellyn, President and Chief Executive Officer

Just to reiterate what Yvan said, our number one deployment strategy is organic growth. And so that's really our number one where we're going to use the excess capital.

Darko Mihelic, RBC Capital Markets

Okay. Maybe will take quite a reversal of fortune to use up capital if it was just organic, unless - in any event, what about the dividend, is it pre-tax provision earnings that will guide your dividend decision?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

I'll take that one as well. So, if I keep going on the asset side, we just mentioned for example, the inventory financing, which is over a billion dollars down. So, we don't see that coming back in the next few quarters, but that will eventually come back. We're pretty optimistic and we like that business. So that's an example of where we're going to use it. As we fix the mortgages, we're going to use some there as well. So, we don't manage the capital on a quarter-to-quarter basis. We do manage on a more medium-term basis where we do envision to increase the assets. In terms of dividend, again unfortunately, I'm probably going to sound like a broken record as Rania mentioned, but this one is prevented by OSFI. So, it's reviewed on a quarterly basis by the board and as they lift restrictions, we will revise what we do. But if you look currently at our payout ratio and adjust the PCL to a more normal level, we would be relatively close to the low end of the pay-out range that we provided to the market. But again, we'll just wait for restrictions to be lifted and re-evaluate that on a quarterly basis.

Darko Mihelic, RBC Capital Markets

Okay. And the pension buyouts this quarter, is that over? I didn't quite catch or understand. Is that complete - and what does it do for you? Does it completely remove all risks around the pension or is it just some sort of longevity risk or is it investment returns? Can you just maybe expand a little bit upon what you did there with the pension risk?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

Definitely happy to take that one, because I think it's a great transaction for the bank and really happy with the outcome. So, what we've done Darko, is that 60% of the obligations of the pension fund was for retirees and roughly 40% for the active employees. So, what we've done is that we bought annuities from a Canadian insurer. This is locked, this is done. And pretty much what we've done is that we took those annuities for 60%. So, for all the retirees of the bank, we now have an annuity that fits perfectly the obligations of the bank. So, we took out 60% of the longevity risk and market risk related to those. So, for us, we feel that's a great way of improving the risk that we can use somewhere else at the bank, not necessarily in our pension plan. And definitely simplify the operation, and everything around it. So, it's a great transaction and we did generate a gain out of it, which is, to be honest, pretty exceptional. So, we were really pleased with the outcome of that transaction.

Darko Mihelic, RBC Capital Markets

Darko Mihelic: Okay. That's good color. Thank you.

Operator

Thank you. Once again, if you would like to ask a question, please press star one. And we'll take our next question from Marcel McLean of TD Securities. Please, go ahead.

Marcel McLean, TD Securities

Okay. Thank you. I actually just want to take a quick look at capital markets. Looks like you guys have materially outperformed the peer group, down only 4%. But if I compare it to pre-pandemic levels of Q1 20, you guys are up about 60% from those levels which is more than double your highest period. I'm just wondering, what's driving your performance? It's not a huge and contributed revenue of only about 10%, but just wondering if this is something we should expect going forward or what's really behind this growth.

Rania Llewellyn, President and Chief Executive Officer

I'll let Kelsey answer that question. Kelsey, go ahead.

Kelsey Gunderson, Executive Vice President, Capital Markets

Thank you very much for the question. I am very pleased with how the business has performed. As you point out, not only in this latest quarter, but since the year began - three big quarters of performance building on what was a record year for us last year as well. You know, we are benefiting from some changes we've made over the last couple of years, in particular realignment of our entire capital markets franchise with the rest of the bank. Something that I don't think was happening as effectively in years past. For instance, we're doing a much better job of aligning our equity and advisory bankers to our commercial lending footprint. And things have been paying off over the last couple of quarters in terms of securing mandates. But a big part of our business remains fixed income and that business has certainly been strong of late. We've seen some good market share gains. And so, it's been what I would characterize as leveraged performance, which has largely been driving what you've correctly pointed out, is some pretty solid performance out of the business.

In terms of sustainability going forward, I think like a lot of others, we expect to see normalization of capital markets activity. We saw a little bit of that in the quarter for us as well, although what I would say is, normalization in fixed income was for us more than offset by good performance in our equities business. But in our business mix, it's tilted towards fixed income and in particular tilted towards government finance. And I think as we all know, the provincial governments are going to need to continue to finance these deficits and we're in an excellent place to capture that business and capture market share. So, I'm optimistic that the performance will continue.

Marcel McLean, TD Securities

Okay. Thank you for that. And then just a second question here moving over to the PCLs. Stage three commercial PCL jumped back up a bit this quarter. I just wonder if there's any trend that's related to specific sectors. If there's anything you want to highlight there that maybe, we should be aware of.

Liam Mason, Executive Vice President, Chief Risk Officer

Marcel, it's Liam. I'll take your question. Thank you for the question on the PCLs. We have seen a slight increase in our gross impaired loans as Yvan articulated. We consider that variation within a normal course of business. And our overall gross impaired loans have been relatively stable. There's no industry concentration per se, we believe that we're adequately reserved. But we do expect that level to decrease as the economy improves based on our disciplined and prudent approach to underwriting.

Marcel McLean, TD Securities

Okay. All right. That's it from me. Thanks.

Operator

Thank you. It appears that there are no further questions at this time. Ms. Llewellyn, I'd like to turn the conference back to you for any additional or closing remarks.

Rania Llewellyn, President and Chief Executive Officer

In closing, I would like to leave you with a few key takeaways.

Our momentum from earlier this year continues into our third quarter. The Bank's capital and liquidity positions are strong, and our credit quality is sound. This quarter also saw some significant achievements including, the recruitment of our new Chief Information Technology Officer, the establishment of our Residential Real Estate Secured Lending group, and the de-risking of our pension plans.

We also remain focused on enhancing the customer experience and driving revenue growth, while continuing to identify structural cost opportunities. We will continue to provide you with updates on our mortgage business and digital roadmap.

Finally, I would like to thank the leadership team and all employees of the Bank as we continue to focus on our strategic plan and charting a new path forward.

We look forward to providing you with an update on our strategic plan by hosting an Investor Day in early 2022. Stay tuned for additional details.

Thank you for joining the call today.

Susan Cohen, Director, Investor Relations

Thank you for joining us today. Should you have any further questions, our contact information is included at the end of the Investor Presentation. Our fourth quarter 2021 earnings call will be held on December 10 and we look forward to speaking with you then. Have a pleasant day.