Conference Call Financial Results

Second Quarter 2022

June 1, 2022

Caution Regarding Forward-Looking Statements

From time to time, Laurentian Bank of Canada (the "Bank") will make written or oral forward-looking statements within the meaning of applicable securities legislation, including such as those contained in this presentation (and in the documents incorporated by reference herein), and in other documents filed with Canadian regulatory authorities, in reports to shareholders, and in other written or oral communications. These forward-looking statements are made in accordance with, and are intended to be forward-looking statements under, current securities legislation in Canada. They include, but are not limited to, statements regarding the Bank's vision, strategic goals, business plans and strategies, priorities and financial performance objectives; the economic and market review and outlook for Canadian, United States (U.S.), European, and global economies; the regulatory environment in which the Bank operates; the risk environment, including, credit risk, liquidity, and funding risks; the anticipated ongoing and potential impact of the coronavirus (COVID-19) pandemic on the Bank's operations, earnings, financial results and financial performance, condition, objectives, and on the global economy and financial markets conditions; the statements under the headings "Outlook", "COVID-19 Pandemic" and "Risk Appetite and Risk Management Framework" contained in the Bank's 2021 Annual Report for the year ended October 31, 2021 (the "2021 Annual Report"), including the Management's Discussion and Analysis for the fiscal year ended October 31, 2021; and other statements that are not historical facts.

Forward-looking statements typically are identified with words or phrases such as "believe", "assume", "estimate", "forecast", "outlook", "project", "vision", "expect", "foresee", "anticipate", "intend", "plan", "goal", "aim", "target", and expressions of future or conditional verbs such as "may", "should", "could", "would", "will", "intend" or the negative of any of these terms, variations thereof or similar terminology.

By their very nature, forward-looking statements require us to make assumptions and are subject to inherent risks and uncertainties, both general and specific in nature, which give rise to the possibility that the Bank's predictions, forecasts, projections, expectations, or conclusions may prove to be inaccurate; that the Bank's assumptions may be incorrect (in whole or in part); and that the Bank's financial performance objectives, visions, and strategic goals may not be achieved. Forward-looking statements should not be read as guarantees of future performance or results, or indications of whether or not actual results will be achieved. Material economic assumptions underlying the forward-looking statements contained in this document are set out in the 2021 Annual Report under the heading "Outlook", which assumptions are incorporated by reference herein.

We caution readers against placing undue reliance on forward-looking statements, as a number of risk factors, many of which are beyond the Bank's control and the effects of which can be difficult to predict or measure, could influence, individually or collectively, the accuracy of the forward-looking statements and cause the Bank's actual future results to differ significantly from the targets, expectations, estimates or intentions expressed in the forward-looking statements. These risk factors include, but are not limited to, risks relating to: credit; market; liquidity and funding; insurance; operational; regulatory compliance (which could lead to us being subject to various legal and regulatory proceedings, the potential outcome of which could include regulatory restrictions, penalties, and fines); strategic; reputation; legal and regulatory environment; competitive and systemic risks; and other significant risks discussed in the risk-related portions of the Bank's 2021 Annual Report, such as those related to: the ongoing and potential impacts of the COVID-19 pandemic on the Bank, the Bank's business, financial condition and prospects; Canadian and global economic conditions (including the risk of higher inflation); geopolitical issues; Canadian housing and household indebtedness; technology, information systems and cybersecurity; technological disruption, privacy, data and third-party related risks; competition and the Bank's ability to execute on its strategic objectives; the economic climate in the U.S. and Canada; digital disruption and innovation (including, emerging fintech competitors); Interbank offered rate (IBOR) transition; changes in currency and interest rates (including the possibility of negative interest rates); accounting policies, estimates and developments; legal and regulatory compliance and changes; changes in government fiscal, monetary and other policies; tax risk and transparency; modernization of Canadian payment systems; fraud and criminal activity; human capital; insurance; business continuity; business infrastructure; emergence of widespread health emergencies or public health crises; emergence of COVID-19 variants; development and use of "vaccine passports"; environmental and social risk; and climate change; and the Bank's ability to manage, measure or model operational, regulatory, legal, strategic or reputational risks, all of which are described in more detail in the section titled "Risk Appetite and Risk Management Framework" beginning on page 50 of the 2021 Annual Report, including the Management's Discussion and Analysis for the fiscal year ended October 31, 2021 which information is incorporated by reference herein.

We further caution that the foregoing list of factors is not exhaustive. Additional risks, events, and uncertainties not currently known to us or that we currently deem to be immaterial may also have a material adverse effect on the Bank's financial position, financial performance, cash flows, business or reputation the Bank. When relying on the Bank's forward-looking statements to make decisions involving the Bank, investors and others should carefully consider the foregoing factors, uncertainties, and current and potential events.

The forward-looking information contained in this document (and in the documents incorporated by reference) is presented for the purpose of assisting investors, financial analysts, and others in understanding the Bank's financial position and the results of the Bank's operations as at, and for the period ended on, the date presented, as well as the Bank's financial performance objectives, vision and strategic goals, and may not be appropriate for other purposes.

Any forward-looking statements contained in this document represent the views of management only as at the date hereof, are presented for the purposes of assisting investors and others in understanding certain key elements of the Bank's current objectives, strategic priorities, expectations and plans, and in obtaining a better understanding of the Bank's business and anticipated operating environment and may not be appropriate for other purposes. We do not undertake to update any forward-looking statements, whether oral or written, made by the Bank or on its behalf whether as a result of new information, future events or otherwise, except to the extent required by applicable securities regulations. Additional information relating to the Bank can be located on the SEDAR website at www.sedar.com.

Non-GAAP financial and other measures

In addition to financial measures based on generally accepted accounting principles (GAAP), management uses non-GAAP financial measures to assess the Bank's underlying ongoing business performance. Non-GAAP financial measures presented throughout this document are referred to as "adjusted" measures and exclude amounts designated as adjusting items. Adjusting items include the amortization of acquisition-related intangible assets, and certain items of significance that arise from time to time which management believes are not reflective of underlying business performance. Non-GAAP financial measures are not standardized financial measures under the financial reporting framework used to prepare the financial statements of the Bank and might not be comparable to similar financial measures disclosed by other issuers. The Bank believes non-GAAP financial measures are useful to readers in obtaining a better understanding of how management assesses the Bank's performance and in analyzing trends.

Non-GAAP ratios are not standardized financial measures under the financial reporting framework used to prepare the financial statements of the Bank to which the non-GAAP ratios relate and might not be comparable to similar financial measures disclosed by other issuers. Ratios are considered non-GAAP ratios if adjusted measures are used as components, refer to the non-GAAP financial measure section above. The Bank believes non-GAAP ratios are useful to readers in obtaining a better understanding of how management assesses the Bank's performance and in analyzing trends.

Management also uses supplementary financial measures to analyze the Bank's results and in assessing underlying business performance and related trends.

For more information, refer to pages 26 and 27 of this presentation and to the Non-GAAP Financial and Other Measures section beginning on page 5 of the Second Quarter 2022 Report to Shareholders, including the Management's Discussion and Analysis (MD&A) as at and for the period ended April 30, 2022, which pages are incorporated by reference herein. The MD&A is available on SEDAR at www.sedar.com.

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 the second quarter 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; Éric Provost, Head of Commercial Banking; Karine Abgrall-Teslyk, Head of Personal Banking, and Kelsey Gunderson, Head of Capital Markets.

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.

I would also remind listeners that the bank assesses its performance on a reported and adjusted basis and considers both to be useful in assessing underlying business performance. Rania and Yvan will be referring to adjusted results in their remarks unless otherwise noted as reported.

As many of you know, several months ago, I made the decision to retire from Laurentian Bank after more than 10 fulfilling years as Head of Investor Relations. During that time, I have had the pleasure of working closely with the investor and analyst community in communicating the Laurentian Bank story. The Bank is entering a new chapter and I look forward to the progress it will continue to make. I would also like to formally introduce Andrew Chornenky who joined the Bank in May as Vice-President and Head of Investor Relations. Andrew has extensive experience in banking and investor relations and has worked closely with the Bank over the last 18 months. I know that he will be a great and collaborative partner with you all.

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

Rania Llewellyn, President and Chief Executive Officer

Bonjour à tous. Thank you for joining us today.

We continued to make good progress against our strategy this quarter. We are confident that our strong, prudent risk culture and disciplined focus on cost management will allow us to manage through the evolving macroeconomic environment, and we expect to exceed our 2022 financial targets.

On behalf of the entire leadership team, I would like to thank everyone at Laurentian Bank. The results this quarter demonstrate their commitment to working as One Winning Team and putting the customer first.

I will now review our Q2 2022 results.

Financial Results

Driven by top line revenue growth of 4% year-over-year, net income for the second quarter was $61.6 million or 9% higher than a year earlier, with earnings per share of $1.39, up 13% year-over-year, leading to our most profitable quarter since Q2 2018. ROE reached 10.3%, up 110 basis points from a year ago and pre-tax, pre-provision income improved by 20% year-over-year. Results were primarily driven by strong performances in Commercial Banking and Capital Markets, and our continued focus on cost management.

Quarter-over-quarter, net income was up 4% and earnings per share increased 10%. ROE was up 110 basis points sequentially and pre-tax, pre-provision income improved by 6%.

With strong revenue growth and our focus on cost management, our efficiency ratio improved to 65.2%, a 470 basis point decrease year-over-year and 180 basis point decrease quarter-over-quarter. Operating leverage was positive at 2.7%.

The Bank's CET1 capital ratio, which is presented under the standardized approach, was 9.3%, compared to 9.8% last quarter. This variance was a result of redeploying capital accumulated during the pandemic and is in line with our strategic plan to invest in profitable, sustainable organic growth.

Given the current macroeconomic conditions and ongoing market volatility, a few additional highlights from this quarter, showcased the continued confidence in our strategy, including:

- The successful issuance of $300 million of covered bonds and $350 million of subordinated debt, leveraging our diversified sources of funding; and
- The confirmation of our long-and short-term credit ratings from S&P with a stable outlook.

We are also pleased to announce a 1 cent increase to the Bank's dividend to $0.45 cents per common share. This is a 13% increase compared to the dividend declared the previous year.

Strategy Updates

As I outlined at our Investor Day, our business lines play a key role in the success of our strategy.

Commercial Banking

Commercial Banking continues to be our growth engine and is executing on a proven business model, highlighted by a record quarter for organic loan generation, led by inventory and real estate financing.

Inventory financing was up by over $800 million or 32% quarter-over-quarter to $3.4 billion, real estate financing grew by over $300 million or 4% to $9.4 billion over the same period, and equipment financing is tracking to plan, driven by strong originations and asset price increases.

Capital Markets

In Capital Markets, we saw a strong rebound in revenues compared to last quarter, reflective of active debt markets and continued progress on our strategy to provide a more focused and aligned offering.

- First, we improved our syndicate position with several provincial borrowers, in line with our objective to grow with core issuers, while also participating in the Government of Canada's inaugural green bond issuance as well as a sustainable bond issuance from the First Nations Financing Authority;
- Second, we achieved our FY 2022 goal to provide coverage to at least 75% of our top-tier commercial clients, up from 50% last year; and,
- Third, we integrated our new real estate research capabilities in our offering, which has led to improved deal pipeline conversion.

Personal Banking

In line with our strategy to reposition for growth with a digital-first approach, Personal Banking continued to make progress in closing key foundational gaps to drive customer retention and acquisition while deepening existing relationships.

- First, the Bank launched a new contactless tap debit card with INTERAC Flash functionality. The launch of the new card closes a key foundational gap and supports the Bank's strategy to drive customer acquisition and enhance the customer experience. The new card continues to give customers access to more than 1 million ATMs across Canada and around the world.

- Second, following our commitment to improve the onboarding experience, we have announced a strategic partnership with thirdstream to enable digital account openings. Rolling out later this year, existing and new customers will have access to a simplified, fully digital application process to open an account in minutes.

- Third, we have reduced redundant systems and processes by more than 60 per cent for mortgage originations so far this year, and we remain on track to meet our 'time to yes' target of 3 days by year end.

Strategy Updates: Culture & ESG

As we said at our Investor Day, our strategic plan is underpinned by a strong culture and commitment to ESG.

Recently, as part of making the better choice, we added four new ESG-themed funds and launched "Green Teams" at the Bank, an employee led initiative to identify low cost and innovative ideas to make our Bank more environmentally friendly.

We have also been taking action to support our employees, including:

- A work-from-home first approach, reducing commuting time and expenses for employees, allowing them to spend more time with their families;
- Providing four summer afternoons off as well as a day off on their birthday for a total of three additional days off per year; and
- The launch of "LifeSpeak", a new mental health resource and wellness platform that provides education and advice on mental health issues. The physical and emotional strength of our One Winning Team is a priority and we believe that maintaining good mental health contributes to personal and professional development.

Our culture is our driving force, and our employees are the biggest stakeholders in our success. Over the past few weeks, we have held a series of employee appreciation events to thank them for their contribution to the Bank. Their energy and ongoing commitment will help fuel our path forward.

Macroeconomic Outlook

I would now like to offer some thoughts on the evolving macro economic environment and potential impacts on the Bank.

Regarding our loan portfolio, we are pleased with our recent results.

Inventory financing is significantly ahead of expectations as a result of three factors:

1. First, OEMs are recovering faster than anticipated from the pandemic and are able to ship more product than expected.

2. Second, the successful growth of our dealer network, which is 20% larger today than it was last year.
3. Third, an increase in the cost of goods driven by supply chain issues and inflation impacting the cost of materials.

Looking forward, we expect a tempering of consumer demand as a result of the current macroeconomic environment and a seasonal volume reduction in Q3 followed by a gradual recovery in Q4.

Turning now to our real estate portfolio. We have a healthy pipeline of $4.4 billion, up from $4.3 billion last quarter. While growth is expected to be moderate, the country is still experiencing a structural housing supply shortage, especially in certain regional markets. Given our specialization in this sector, we continue to support our long-term, top-tier clients as they work to meet demand. In speaking with them, they see further opportunities as a result of future immigration waves, which will lead to sustainable population growth in Canada, and the continued need for more housing.

As we look to the residential mortgage sector, we expect loan growth to moderate in this rising rate environment. With a potential cooling period, it enables us to continue to make the strategic improvements we laid out at our Investor Day to enhance the customer experience, and better positions us to capitalize on future growth.

Across our loan book, our underwriting practices are strong, and our portfolio is highly collateralized. We take an extremely disciplined approach in dealing with uncertainty and remain adequately provisioned to weather the rapidly changing environment.

Conclusion

Before I conclude my opening remarks, I would like to personally thank Susan Cohen for her dedication to the Bank leading Investor Relations for the last 11 years. She has played an important role over that time in establishing strong relationships with our analyst and investor community and we would like to take this time to wish her all the best in her retirement.

I am also pleased to welcome Andrew Chornenky to the Bank. His background and extensive experience in banking and financial communications will be an asset as we continue to execute on our strategy. He knows the Bank very well and I know he is looking forward to meeting and working with all of you.

I would now like to turn the call over to Yvan.

Yvan Deschamps, Executive Vice President, Chief Financial Officer

Merci, Rania et bonjour à tous.

I would like to begin by turning to slide 12 which highlights the Bank's strong financial performance for the second quarter of 2022.

Reported EPS was $1.34 and net income was $59.5 million. Adjusting items this quarter amounted to $2.8 million before taxes and included $3.1 million related to the amortization of acquisition-related intangible assets and a favourable adjustment of $0.3 million to the provision related to premises. In December 2021, we estimated the charge related to the sub-leasing of our corporate office spaces and for the write-off of the related leasehold improvements. On a quarterly basis we review and update our estimates. As a result, there may be further adjustments, including, once the subleases are finalized. Details of adjusting items for the quarter are shown on Slide 26. The remainder of my comments will focus on adjusted results.

EPS and ROE were $1.39 and 10.3%, an increase of 13% and 110 basis points respectively compared to a year ago, and ahead of our 2022 financial targets. The pre-tax pre-provision income (or PTPP) was $90.3 million, a 20% increase compared to last year, driven by both strong revenue growth and a reduction of non-interest expenses.

Compared to the first quarter of 2022, EPS and ROE increased by 10% and 110 basis points respectively, mainly from sustained commercial loan growth, other income related to financial markets and continued cost management. PTPP increased by 6%.

Slide 13, shows the net interest margin. At 1.87%, NIM was relatively flat, down 1 basis point year-over-year and quarter-over-quarter, as the improved commercial banking contribution was offset by a lower contribution from personal banking.

Regarding rising interest rates, as outlined by the sensitivity analysis in the MD&A, a 1% parallel rate increase on the yield curve would have a positive impact of $12 million on NII over the next twelve months.

Other income, as presented on Slide 14, increased by 2% compared with a year ago and 4% sequentially, mainly due to a strong performance in financial market related revenues, being fees and securities brokerage commissions, as well as income from financial instruments.

Slide 15 presents non-interest expenses that decreased by $5.3 million or 3% compared to a year ago. This was mainly due to lower amortization charges and rent expenses resulting from the strategic review and our decision to reduce our corporate office footprint by 50%. Partly offsetting this decrease were regular salary increases and the higher level of performance-based compensation related to the Bank's improved performance. Sequentially, non-interest expenses decreased by 2% due to lower premises and technology costs, as well as cost discipline in other expenses.

The efficiency ratio this quarter stood at 65.2%, an improvement of 470 basis points year over year. Sequentially, the efficiency ratio improved by 180 basis points. As a result of revenue growth and our focus on cost discipline, the efficiency ratio has exceeded our expectations this quarter. Given our strategic investments to close key foundational gaps and improve the customer experience with a digital-first approach in Personal Banking, overall spending will increase in the second half of 2022. Operating leverage was positive at 2.7%.

Slide 16 presents our diversified sources of funding. In the last two quarters, deposits increased by 9.8%, or $2.3 billion, and loans grew by 6.6%. Sequentially, deposits grew by 4.7%, or $1.1B, while loans grew by 4.3%. The deposit growth tracks positively with our objective to grow deposits in line with asset growth on a relative basis. Growth in personal notice and demand deposits reflects our ongoing strategy to deepen and expand relationships with advisors and brokers.

Slide 17 highlights our capital position. The CET1 capital ratio, which is presented under the Standardized approach, stood at 9.3% at the end of the second quarter compared to 9.8% last quarter. This quarter's variation was directly linked to the redeployment of accumulated capital during the pandemic to sustainable, profitable commercial loan growth in line with our strategic plan.

Considering the current macroeconomic environment and in line with our disciplined approach to capital, we have taken the prudent step of pausing our activities to repurchase additional shares as part of our normal course issuer bid. To date we have redeemed 401,200 common shares, or about half of our entire program. We will continue to monitor the macroeconomic situation and reassess the program throughout the rest of the year. Given our prudent approach, we are confident that our internal capital generation will sustain loan growth for the remainder of the year.

Slide 18 highlights the commercial loan portfolio which delivered strong growth. Loans increased by $1.3 billion or 9% quarter-over-quarter, driven by growth in inventory financing of over $800 million or 32% and real estate financing of over $300 million or 4%.

As Rania mentioned, the ability for OEMs to ship more product, the growth of our dealer network and the increase in the cost of goods, outpaced the expected normal seasonal volume reduction in inventory financing this quarter.

Slide 19 presents the pan-Canadian residential mortgage loan portfolio. Residential mortgage loans increased by 1% sequentially. We previously mentioned that improving the performance of the mortgage business is expected to be gradual, and we continue to take actions to improve the customer experience, retain customers, and renew growth.

The Bank's residential mortgage portfolio remains relatively weighted towards insured mortgages at 56% when compared to the industry and combined with a low LTV of 44% on the uninsured portfolio, contributes to reducing the overall risk of this business despite the changing macroeconomic environment.

Turning to Slide 20, allowances for credit losses totaled $196.9 million, a sequential decrease of $12.0 million, mainly due to write-offs of previously provisioned accounts in the commercial loan portfolio.

As shown on slide 21, the provision for credit losses was $13.0 million in the second quarter of 2022, increasing by $10.6 million from a year ago. This was mainly due to releases of provisions on performing loans of $9.9 million last year. Sequentially, the provision for credit losses increased by $3.6 million due to volume growth in commercial loans and changes in the macroeconomic outlook. The PCL ratio stood at 15 basis points.

Slide 22 highlights the improving trend in gross impaired loans which decreased by 12% quarter-over-quarter, mainly due to write-offs of previously provisioned accounts in the commercial loan portfolio.

We have a prudent and disciplined provisioning process which includes setting reserves that allow us to be responsive to changing macroeconomic conditions. We further stress test the portfolio against various scenarios, and this quarter, given the heightened level of uncertainty, we increased the severity of our pessimistic scenario and its weighting in setting our ACL. Given the level of uncertainty in the market we continue to manage our risk with a cautious approach and remain adequately provisioned.

I would now like to offer some thoughts on how we see the remainder of the year developing.

- We expect revenue growth to continue in Q3 as a result of three additional days in the quarter, as well as tailwinds from recent commercial loan growth.
- NIM is expected to move north of 1.90%.
- We anticipate continued good performance from our Capital Markets business line but remain cautious as uncertainty and market volatility remain elevated.
- Our focus on cost discipline will continue. Overall spending is expected to increase in the second half of 2022 as we deliver strategic initiatives to improve the customer experience in Personal Banking and invest to support our growth. Despite the anticipated increase, we expect to remain below our 2022 efficiency ratio target of less than 68% leading to a positive operating leverage for 2022.
- The provision for credit losses remains difficult to predict on a quarterly basis given the macroeconomic environment.
- We efficiently redeployed previously accumulated capital into profitable organic growth during the quarter, leading to an improvement of our financial results. We now expect more tempered growth for the balance of the year with internal capital generation expected to sustain loan growth during the second half of the year.

As a reminder, next quarter, the semi-annual LRCN interest payment will impact EPS by 6 cents.

Despite the current environment and related uncertainties, we expect that the strong results delivered in the first half of the year position us to exceed our 2022 financial targets.

I will now turn the call to Andrew Chornenky.

Andrew Chornenky, Vice President and Head of Investor Relations

Good morning. Thank you, Rania, and Susan, for your introductions. Susan, I would like to wish you all the best in your retirement. To those of you on the call, I look forward to introducing myself either in person or virtually over the coming weeks and working with you in the future. At this point, I would like to turn the call over to the conference operator for the question-and-answer session.

Operator

Thank you. If you wish to ask a question at this time, please signal by pressing star one on your telephone keypad. Please ensure the mute function on your telephone is switched off to allow your signal to reach our equipment. Again, please press star one to ask a question. I will pause for just a moment to allow everyone an opportunity to signal for questions.

We can take our first question now from Meny Grauman of Scotiabank. Please go ahead.

Meny Grauman, Scotia Global Banking and Market

Hi. Good morning. I wanted to start off just by asking a question about loan growth, commercial loan growth up very strong sequentially and year over year. I'm just wondering if you could break that out between increases in line utilization versus new business, how that would break out in terms of the growth?

Éric Provost, Executive Vice President, Commercial Banking and President, Quebec Market

Thank you, Meny, Eric, here. It's a good question. Our utilization right now is at 50%, so closer to the mid-50s we guided you towards and significantly above the mid-30s we've experienced last year. And like mentioned in the opening remarks, the team did a great job in terms of growing our dealer base over 20% year over year. So, I'd say those are the biggest drivers for that growth increase in inventory financing. We're seeing more of a trend towards normalization at that portfolio from what we've experienced prior to the pandemic situation.

Meny Grauman, Scotia Global Banking and Market

So just specifically digging into that inventory finance business, I just wanted to clarify relative to the expectations that you provided when we spoke on the back of the Q1 results, just what's happening there? I know you spoke to it a little bit but just to clarify in terms of clearly the environment is better than you expected, so is that sustainable. And in terms of the seasonality that we would typically see, is that something that is going to be observable in Q3, or are the bigger growth trends going to - are they going to not make that observable in Q3 either?

Éric Provost, Executive Vice President, Commercial Banking and President, Quebec Market

What we expect is really a volume reduction in Q3 due to the seasonality of the product. So we expect some reduction, but that will be followed by a gradual recovery in Q4 in terms of growth. The big, big driver is the fact that some OEMs are just recovering faster in terms of the supply chain and they're able to replenish the dealerships. But again, in terms of line utilization, at 50%, this is pretty much where in normal trends, we should expect the dealers to be right now. We're very comfortable where we are and we expect seasonality to have, again, an impact this year for Q3 in terms of volume reduction there.

Rania Llewellyn, President and Chief Executive Officer

So maybe if I can just add to Eric's comments. As we said in all of our remarks, the results this quarter did exceed our expectations so based on the guidance that we provided the last quarter, this did exceed our expectations. And primarily driven, like we knew we had grown our dealer network, we said we put the pipelines in place, the OEMs recovering faster was really kind of the biggest driver here in addition to the increase in the cost of goods. But as Eric mentioned, in terms of the utilization, we're going back to pre-pandemic levels. In terms of the Q3 forecast, as Yvan mentioned in his remarks, we're likely going to see a small seasonal reduction in Q3 which is why we're still forecasting that revenues are going to continue to grow because of that tailwind in commercial, with a gradual recovery in Q4.

Meny Grauman, Scotia Global Banking and Market

Got it. So just putting it all together in terms of overall loan growth, so it seems pretty reasonable that the utilization piece has largely run its course. And so, going forward, is it reasonable to expect a moderation in loan growth just because utilization is not going to be a driver - as much of a driver as it has been?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

This is Yvan. For the second half of 2022, definitely you should anticipate that the growth is going to temper and that's impacted by what we just discussed. So that's also why the internal capital generation is going to sustain it or even more than sustain it for the next six months. And next year, we're also going to restart the growth in that portfolio with normal seasonality that we're going to see, but for the second half, expect a tempering of that growth.

Meny Grauman, Scotia Global Banking and Market

Got it. I guess you pre-empted my question on capital, but maybe I'll just ask. We've seen one of your peers tap an ATM to help fund growth, is an ATM something that you would consider if growth exceeded your expectations once again, is that something on the table for you?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

Since you open the capital topic, Meny, I'll just use a few messages and finish by answering your ATM question. We have a solid capital base, right now, we're at 9.3% CET1. We do manage capital prudently, and as a reminder, we always stress that we're under the standardized method which is important to note for some investors. Our objective is to manage above 8.5% so we're still quite above that level. As a reminder, pre-pandemic, we were at 9% so we're still ahead of where we were pre-pandemic. The pandemic caused deceleration or reduction of some portfolios. We had to catch up. We've seen an increase and now recovery of that portfolio but we're still at a good place in terms of capital. Our first priority has always been and remains to deploy that capital through organic growth and that's what we've seen over the last six months. And that definitely contributed to the improvement of the financial statements.

As I mentioned, we expect now tempered growth for the remainder of the year and the internal capital generation to cover that, which leads to finishing the year probably around the same level or slightly a little bit up depending on what's going to happen exactly. So to answer your question, the ATM is definitely part of any toolbox in terms of management of the capital. But at this point, based on the comments I just provided, we're comfortable with the level and we don't anticipate having to use that.

Meny Grauman, Scotia Global Banking and Market

Thanks for that. Thank you.

Operator

We can now take our next question from Doug Young of Desjardins Capital Markets. Please go ahead.

Doug Young, Desjardins Capital Markets

Hi. Good morning. Just going back or going to net interest margins, given the pickup quarter over quarter and commercial loan balances and decline in the personal side and deployment of capital and deployment of funding and whatnot, I would have expected NIMs to be actually up sequentially. Is this - is there something else going on here in terms of asset yields or competitive pressures or funding costs? Hoping you can just kind of maybe elaborate a bit.

Yvan Deschamps, Executive Vice President, Chief Financial Officer

Yeah, it's definitely a good question. And what I can do is explain a bit, give you a bit more color, as well as a bit of guidance going forward. The NIM was relatively stable this quarter. The higher commercial loan growth definitely contributed favorably to it but as I mentioned and used in my comments for personal, but I will generalize that, there was definitely the impact of higher funding cost this quarter and a very competitive pricing environment for all the banks, so not just for us. On the funding side, for example, in a rising rate environment, what happens is, as an example, is the CDOR rates are going to move faster based on anticipation and the prime rate is going to move after when the rates increase.

So that delay is something that kind of delayed the recovery of the NIM. But we now expect that for the second half, we're going to be north of 1.90 and a few basis points probably above that 1.90. We will see the tailwind of that growth fully kicking in over Q3. And depending on the level that we will experience in the portfolio mix in Q3 that should be sustained in Q4.

Doug Young, Desjardins Capital Markets

Just a follow-up on that, is that because the delayed prime increase is starting to kick through post the funding costs going up, is that the main driver that's pushing it up over 190 in Q3?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

There's two impacts, definitely, that is an example. We've been competitive from a funding perspective as well because we have strong growth and we have to sustain it. But what you see also is that the full growth or the full impact of that growth usually kicks in the next quarter because there's half of a quarter and then you get the full benefit the next quarter. So that's really for the remainder of the year, that will be north of the 1.90, and that you'll get the full benefit.

Doug Young, Desjardins Capital Markets

And that's factoring in, in terms of bank counter or rate cuts, obviously, there's been one already. Is that factoring in two more additional rate increase, sorry, increases?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

At this point, we're all looking at rates including today. Everybody is expecting a rate increase. On the rate increase, we mentioned in the MD&A that currently, the way we were positioned at the end of Q2, a 1% increase parallel - increase on the rate curve would be equivalent to $12 million. So, depending on how the rates evolve towards the end of the year, there'll be an additional kick in the NIM and in the NII as well. But we will see probably most of it kicking towards the end of the year and next year. Not necessarily instantly.

Doug Young, Desjardins Capital Markets

Okay. So that's not in - the Bank of Canada's future rate increases is not in your above guidance?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

It's partly included, but again, it depends where it's going. Everybody expected now it's leading towards the neutral zone, the 2% to 3% but towards the end of the year. And we all know or expect today there's probably going to be an increase which will gradually benefit. But as I mentioned, there's a question of repricing of the assets, there is a timing of all of that. So it will be a gradual benefit over the next few quarters and with the main or the full contribution in 2023.

Doug Young, Desjardins Capital Markets

Okay. And then just I'm hoping you can unpack a bit of what's in other income. Specifically, the income from financial instruments was a big increase and I think there was a mention of capital markets a few times. Have you disclosed like how much capital markets contributes, or would you disclose how much capital market contributes to pre-tax pre-provision earnings? Or what was the quantum of the benefit you got from capital markets into your results this quarter? And was that a big part of what's in that income from financial instruments line?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

The increase this quarter is mainly related to what we describe as other income-related financial markets. We don't disclose the segment, so there is no segment called Capital Markets, and we don't disclose that. But as we had done in the Investor Day, what we give as a proxy is two categories that the other income fees on the fixed income deals and things like that. So, Kelsey is going to go through that as well as income from financial instruments. I'll pass it to Kelsey that will provide more color.

Kelsey Gunderson, Executive Vice President, Capital Markets

Thanks, Yvan. We're pleased with the quarter in capital markets, especially in the context of what was a pretty volatile market. As everybody knows, for us, our fixed income business continues to perform really well. We saw good capital markets activity in the quarter, particularly with our core customers. As we've talked about through the last quarters and in the Investor Day, and as Rania mentioned in her opening remarks as well, we continue to align our entire capital markets franchise with our - with the rest of the bank and in particular commercial as well. And again, as Rania mentioned in her opening remarks, we've improved our coverage of our commercial clients from 50% to 75% over the last little while as well.

So really good performance there, and in particular as well, actually, I should mention too that as Rania rightly said in her opening remarks, we've improved our syndicate positions with each of our issuers, in particular the government issuers. So a really good quarter for us, I'm pleased with the results.

Doug Young, Desjardins Capital Markets

So just clarify and then I'll stop asking questions. But the capital markets goes through the fees and security broker commission line and then the income from financial instruments is separate from capital markets, is that right?

Kelsey Gunderson, Executive Vice President, Capital Markets

Yeah. Those are the two main lines.

Doug Young, Desjardins Capital Markets

And then income and financial instruments, like what was the big driver within that? Because it was up 57% year over year. I guess my question is, what's in there, what - is this sustainable?

Kelsey Gunderson, Executive Vice President, Capital Markets

Those are obviously market to market adjustments on inventory positions as well. I think it's probably worth pointing out we don't run large inventory positions here, we've been evolving our business away from what you probably consider trading strategies to more fee-based strategies. And I described the rationale for that a minute ago. But the percentage increase, quarter over a quarter, is certainly large, but the absolute dollar amount is not particularly large. We typically run that line somewhere between $5 and $6 million per quarter. We are on the high end of that this quarter and - but I think that's probably a sustainable level to think about going forward.

Doug Young, Desjardins Capital Markets

Perfect. Great. Thank you.

Operator

We can now take our next question from Paul Holden of CIBC. Please go ahead.

Paul Holden, CIBC

Thank you. Good morning. I want to ask you some non-related questions, but from a little bit of a different angle on that relates to bank account openings and sort of growing those low-cost deposits, which are obviously becoming increasingly important given the trends you talked about for deposit costs. So maybe some thoughts there, because I also know in terms of execution on your strategic plan, you're on track on most objectives, and one where you're falling a little bit behind is new bank account opening. So maybe you can address that. And it's becoming of increasing importance to.

Karine Abgrall-Teslyk, Executive Vice President, Head of Personal Banking

Thank you, Paul, for your question, it's Karine. So, as you know, deposits are core to our bank and really a key focus in our strategic initiative. As shared at Investor Day, we were focusing on three key segments, one of them being deposits and then credit cards and mortgages. We're well-positioned to compete in the market through the competitive rate. And we announced a strategic partnership, with Third Stream, which is really going to allow us to enable digital onboarding and further drive deposit growth. So we'll have an opportunity to grow nationally outside of Québec. We've also introduced a loyalty team which is really setting us up for good progress in terms of proactively reaching out to customers in order to retain their deposits. But we need to continue to improve as we build digital capabilities. Our account opening target is what's really a stretch that we've established, and it's aligned to our digital journey. So, it's really just a question of timing. So, we believe that we're building the right foundation for growth.

Paul Holden, CIBC

Okay. And when you say it's a question of timing, how should we be thinking about that timing given you going to launch the thirdstream partnership sort of the back half of this year? Is it reasonable to have expectations then that branch-raised deposits should start to accelerate in 2023 or might it take longer than that?

Karine Abgrall-Teslyk, Executive Vice President, Head of Personal Banking

Yeah, that's a fair assumption that you're making, because overall the key message is really around the foundational gap that we're closing this year. So this year is the year of stabilization and we're focused on the customer acquisition and retention pieces and improving the customer experience. So as a digital-first approach and journey mapping keep on happening and being delivered this year, we're going to see key benefits as we progress.

Paul Holden, CIBC

Okay, great. And then a final question on this topic, any kind of sense you can give us on what those digital deposits might cost in the funding perspective versus the broker-based deposits? Is there a significant spread between the two? I imagine there is, but just want to verify.

Yvan Deschamps, Executive Vice President, Chief Financial Officer

I wouldn't say there's that much difference between the two, In fact, the rates are public. So you can see that. And you're going to see they're relatively along with the short-term deposits. So at this point, I wouldn't say it is material and the amount is starting to be relatively small, what we have right now in digital, because we're changing the platform and we're changing that project as well. So that base, we let it run up a bit this year as we transition to the new technology, the new platform, the digital onboarding that Karine is doing. And next year, we're going to revisit exactly what's our strategy with those deposits.

Rania Llewellyn, President and Chief Executive Officer

And Paul, just a reminder, so right now, to a certain extent, the majority of our deposits are kind of - on the retail side are kind of Quebec based. With the digital onboarding platform, that gives us now a new platform to be totally pan-Canadian, and it's fully self-serve in terms of account opening. So we're very excited about delivering that solution at the end of the year and reaping the benefits in fiscal 2023.

Paul Holden, CIBC

All right. One last question on a different topic. You talked a little about the inflationary impact on some of your customers, particularly inventory finance. I'm wondering if there's any particular risk you're seeing or thinking about in terms of inflationary impacts on your commercial customers from a margin or profit perspective.

Éric Provost, Executive Vice President, Commercial Banking and President, Quebec Market

Well, Paul, we're highly specializing in our industries, and right now, yes, there are some inflation pressures, but like from our perspective in terms of how we underwrite, how we go to market, we're very cautious and prudent. And what we hear from customers that they are planning and making sure that they provide either contingency or some reserve on those potential increases in prices. So we feel good about where we are in the portfolio and think that that can be managed throughout our underwriting processes.

Rania Llewellyn, President and Chief Executive Officer

Yeah, well said, Eric. I mean Paul, we factor, as Eric said, into our underwriting process, the rising construction and high cost of inflation in commercial real estate, the increased debt service into the leveraged finance and syndicate portfolios. And we're really very focused on how that will impact the customer and managing to prudent LTV metrics and assessing, as Eric said, the contingency levels in the files. So with real estate, you factor in your contingencies when you're underwriting. We're comfortable with where the portfolio is and managing to support our customers.

Paul Holden, CIBC

Okay. That's good. I'll leave it there. Thank you.

Operator

We will now take the next question from Nigel D'Souza of Veritas Investment Research. Please go ahead.

Nigel D'Souza, Veritas Investment Research

Thank you. Good morning. I had a question for you on the funding side. When I look at your term deposits this quarter, they were up by $1 billion, and last quarter, I believe they declined by $1 billion. I know that's year over year, but are you seeing a shift in preference away from notice and demand to term in a rising rate environment? And are you also seeing a shift maybe towards the advisor and broker channel in a rising rate environment? Which outlook on the funding side and how does that impact your NIM outlook?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

Thank you for your question. On deposit, I would say there is a big change of strategy between this year and last year. Last year we were optimizing the funding of the bank and we used securitization much more. So I'll just push that aside and I will focus on what's been happening this year. This year, over the last six months, as I mentioned, we've been highly successful in terms of growing our deposits and really pleased with the performance. On the demand deposits, we grew and added relationships and that's been a very big contributor to the growth that we had, so very pleased with that. On the term deposits, we've been active. In fact, in the branches, we did increase the rates and got good success at stabilization of that base, which is the objective that Karine discussed a few minutes ago, for this year.

From a broad broker perspective, we've been active in the market, pretty competitive to sustain the growth of the bank. And what we're seeing is that the market is slightly shifting longer on the curve. But I wouldn't expect that that's going to drive much on the NIM side because if you factor all the elements on the funding, we do hedge the balance sheet and we do align the terms of the funding and the assets. So at the end, treasury is going to realign all of that. But definitely from a deposit perspective, the longer we get the term deposits, the more positive it is for us because you don't need to renew it constantly. Which has been the trend for the last few years with shorter-term deposits, like a one year was the key term deposits that people were getting in the market. But we feel, and what we hear from customers and our advisors right now, is that longer-term deposits are starting to get some traction. But as the interest rates continue to increase, we will probably continue to see that trend. But again, from a NIM, I wouldn't put too much on this, we do manage at the bank level the overall balance sheet.

Nigel D'Souza, Veritas Investment Research

Okay. That's really helpful. Thank you. That's it for me.

Operator

We will now take the next question from Jay Kim of Crédit Suisse. Please go ahead.

Joo Ho Kim, Crédit Suisse

Hi. Good morning. I wanted to ask on inflation but from an expense perspective. Just wondering if you're seeing any inflationary pressure from wages just given some of the commentary this quarter we saw from your larger peers on rising salaries and benefits. Wondering if you could give us a bit of color on what you're seeing from an inflation and wage perspective there? Thank you.

Rania Llewellyn, President and Chief Executive Officer

Thanks for the question, Joo Ho. What I would say is that we continue to be focused on cost discipline, that's something that we embedded into the culture over the last 18 months. But just a reminder, cost discipline is only one aspect of it. We've also started to cost optimize structurally our organizations. If you actually look at our expenses year over year, we're down 3%, we're down 2% quarter over quarter. And so while everyone is experiencing some inflationary pressures, we have lots of levers that we can pull on and it's something that we're dynamically managing our expenses. So it's really finding that right balance between investing in the future while being prudent. And as Yvan mentioned in his opening remarks, the second half of the year, expenses will likely go up to continue to deliver on our key strategic priorities, primarily brim Visa transformation and onboarding.

But what we can guarantee, and that's what we're very confident about at this point in time, is that we'll maintain our efficiency ratio below 68% with a positive operating leverage. In terms of your question around just in terms of compensation and salaries, salaries have gone up, like I said, everybody is impacted by inflation. But when we look at the war on talent out there, we view salaries as just one small aspect of what the employee experience and total compensation is. And so to put that in perspective, despite the war on talent, we've been able to attract top talent since November 1st, representing almost 20% of our overall employee base. And that's a factor for a number of things.

We've really differentiated ourselves in the market by offering our employees a work-from-home first approach, and that's given them flexibility. And in this current macroeconomic environment, it's actually created some real cost savings for our employees. So they don't need to commute, they're not paying - they're not spending as much on gas, they're not spending much on in terms of work clothes. We've given them some summer afternoons as well as their birthday off, so additional time off. And then most recently, the new mental health resource life speak that we launched. And we're further comforted by the fact that we hosted 1000 of our 3000 employees over the last three weeks at different appreciation events in Toronto and Montreal. And they told us, it's - the cultural shift is helping drive that renewed sense of pride, their productivity, and their commitment to the overall organization.

But as any good employer, we're constantly reviewing our compensation packages to make sure that we are competitive, and that employee experience is competitive. And we'll continue to benchmark, but we're very comfortable in terms of our ability to pull the right levers and manage our cost appropriately.

Joo Ho Kim, Crédit Suisse

Thank you, that's very clear. Just lastly from me, just on credit, I'm just looking at the performance this quarter, I think we saw some of the peers, I guess, see a similar increase to the adverse scenario rating. But parts of that, I guess, impact being offset by positive credit migration. Wondering if you could give a bit more color on sort of the moving parts and the performance build this quarter if there's any? Thank you.

Liam Mason, Executive Vice President, Chief Risk Officer

Sure. Thank you for the question. Q2 2022 PCL of $13 million or 15 basis points is really in line with normalized run rate of PCLs given the portfolio mix. We continue to see good underlying credit quality in the portfolio. The growth in PCL was mainly due to commercial volume growth, but we did increase our performing ACL due to the changes in the macroeconomic outlook. We take a prudent conservative approach to setting ACLs. We did increase the weighting on the pessimistic scenario and we adjusted the conservatism of our forecast and the economic scenarios based on the forward-looking. And I should note that ACL is a forward-looking economic outlook based on GDP, higher inflation, housing pressures, unemployment. And so we're going to continue to drive a prudent, measured, reserving approach going forward. And I hope that gives you the components, but top line, volume, but also appropriate conservatism given the macroeconomic forward environment.

Joo Ho Kim, Crédit Suisse

Thank you very much.

Operator

We will now take the next question from Sohrab Movahedi of BMO Capital Markets. Please go ahead.

Sohrab Movahedi, BMO Capital Markets

Thank you. Just two clarifications. Liam, just on the answer you gave, so was there – can you talk about whether or not there was any negative migration in the overall portfolio or was it net positive migration, or was it just portfolio size growth?

Liam Mason, Executive Vice President, Chief Risk Officer

From a stage migration perspective, Sohrab, I did not see new adverse formations. We haven't seen a lot of stage migration, relatively stable. To give you some context, 95% of our portfolio is in stage one, 4% stage two, we're really we're not seeing adverse formations that reflects sort of current economic environment which is really quite strong. It's the forward-looking element that is driving our prudence in setting the ACLs.

Sohrab Movahedi, BMO Capital Markets

Okay. And just for maybe an abundance of clarity, because you're still standardized, any portfolio quality degradation wouldn't necessarily show up in RWAs, is that fair?

Liam Mason, Executive Vice President, Chief Risk Officer

It would not show up in RWAs but it would very much show up in our ACLs. And so the key for me is always about that prudent, measured approach to ACLs. And unlike some of our competitors, we took the stance of looking at that forward economic outlook. We don't think it is as strong as where we are today and we're being prudent and measured in taking additional reserving steps and increasing our reserves for it. And we will continue to operate that way.

Sohrab Movahedi, BMO Capital Markets

And then just, you provided a relatively detailed, I guess, roadmap or dashboard on how you are tracking relative to some targets that, financial and otherwise, that you've got out there. Is it the intention to provide this every quarter with an update to it?

Rania Llewellyn, President and Chief Executive Officer

So, Sohrab, in the appendix of the investor presentation, there is an appendix that actually tracks every KPI and we have been presenting that every quarter. So that's our intention. By the end of the year, as we're going into profit planning season for next year, we will be looking to revisit those and we'll obviously share that at the end of the year as well in terms of what we're going to be tracking to next year. But it is available on the appendix on a quarterly basis.

Sohrab Movahedi, BMO Capital Markets

Perfect. Thank you.

Operator

And we can now take our next question from Lemar Persaud of Cormark. Please go ahead.

Lemar Persaud, Cormark

I just want to come back to your opening comments on the strength in inventory, finance, and specific inventory financing, and specifically the 20% year-over-year growth in the dealer network, and really just questioning the 20%. That seems like a big number but maybe it's because you're going from a really small base so that 20% isn't really that large. So maybe if you could offer it, how many additional OEMs specifically was that 20% growth made up of? Like maybe you went from ten to 12 relationships so 20% is only two additional relationships. So any color there would be helpful.

Éric Provost, Executive Vice President, Commercial Banking and President, Quebec Market

Thank you for the question, it's a good question. But no, actually a theme executed quite strongly on onboarding new programs and new dealers. And when we're talking about increasing dealer base, it's really at the dealer level. So we went from just over 4,200 dealers to now servicing over 5,000 across North America. So we definitely saw very strong organic work throughout our dealer base from the team and inventory financing. And we service close to 500 plus OEMs into various types of products. So no, I would just say that it's really good work from our inventory finance team and it's a result of our strong specialization there.

Lemar Persaud, Cormark

That's good, that's good color. So brings me to my next question, what's the outlook for continued growth there? Is 20% for the next few years a reasonable expectation or is this more of a one-off? And I guess I'll tell you where I'm going with this. I think one of the comments you guys have made in the past was that as you add more relationships, it should over time reduce the impact of seasonality. So that's why I'm interested to see if you guys can - first of all, is that true? And then secondly, can you continue to add years of 20% growth such that seasonality in a couple of years is not something that comes up in the Q&A for your conference calls.

Éric Provost, Executive Vice President, Commercial Banking and President, Quebec Market

Yeah. Again, it's a great, great question. As we mentioned at our Investor Day, we intend to diversify the portfolio. When we've acquired Northpoint in Commercial Finance and still now, there's a strong focus into RV-type dealers as well as Marine. So that accounts for about 60%. And the expertise we have there and the deployment of our sales force really makes us very successful into winning market shares. But as we said, like we want to diversify in technology, agriculture, small construction equipment, and some also green type products, EV products. So right now the team is building that specialized approach so we should expect to grow those dealers. We grew maybe 30 dealers in those segments in the last quarter. So overall, we feel that we have good momentum and focusing sales force towards those less seasonal type industries will reduce seasonality.

In terms of pace, I think that the team did a great job. It's hard to predict the pace of dealer growth, but we feel that we have good momentum and this is a growth focus for us in terms of segment and we'll continue to pursue that.

Lemar Persaud, Cormark

I think that's helpful, and then maybe I'll leave it there about that. And just coming back to one of the answers earlier, I think I heard that line utilization is in line with normal trends. What would prevent it from going above pre-pandemic trends?

Éric Provost, Executive Vice President, Commercial Banking and President, Quebec Market

Well, actually pre-pandemic, if we go back to Q2, just before Q2 2020 was - utilization at that time was around 58%. So during the low season right now, we run at about 50% utilization, which for us, it's not a question of going up or not, it really depends on the type of products on the line and the ability of the OEM to replenish the dealers as per their forecast of their sales season. So again, if we diversify that portfolio, you will see a more normalized type utilization which should average mid to high 50s, but not being a hard number. It will always depend on the economic macro environment and that is very hard to forecast or to predict.

Lemar Persaud, Cormark

Okay. Great. Thanks. That's it for me.

Operator

And we can now take our next question from Gabriel Duchesne of National Bank Financial. Please go ahead.

Gabriel Duchesne, National Bank Financial

Good morning. I apologize if I asked something that's already been asked because I got some technical difficulties during most of the Q&A here. But good quarter, very encouraging guidance. I have a question on the capital, you're indicating you expect it to be flat-ish from here on out, but what if loan growth continues to surprise the upside? Like, what's your minimum comfort level for capital? And is there any thought towards some strategies to maybe enhance your capital position, if like one of your peers does an ATM program? And I don't know if that's crossed your mind at all?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

That question was asked but no problem, it's an important one. It's my pleasure to give you the same color. So we definitely manage the capital prudently, then as a reminder, I always remind that we're on the standardized approach. We're currently at 9.3 CET-1, we mentioned that our objective was to remain above 8.5 so there's still a good cushion in place. And the second thing is that, as I mentioned a few minutes ago, is that pre-pandemic we were at 9%. So people kind of forgot that there's been an increase of the capital that was due to a slowdown of some portfolios. We're seeing the catch-up over the last few quarters so we're getting back to a more normal level in terms of what we had been running pre-pandemic. And that's great because we've been able to redeploy capital through organic growth, which is the redeployment of the capital accumulated during the pandemic.

But that contributed a lot to the financial results which are pretty good, as you can see this quarter. For the remainder of the year, we had mentioned that the growth is going to temper and a portion of that is what Eric just mentioned about the seasonal reduction inventory financing. So for the remainder of the year, we would expect that the capital - internal capital generation is going to sustain the capital or slightly improve it. So there's no stress at this point. We're pretty comfortable with the levels. We will reassess and provide more guidance at the end of the year going forward in terms of growth. But the key point that Eric just mentioned is we're not yet back to a historical level of utilization, but we're getting closer and we're expecting that the last probably shot of catch up that we need to do is going to be more gradual than what we've seen over the last two quarters.

So we're pretty comfortable, and if you refer to the ATM program at this point, based on the comments I just gave, it's one of the elements you would use and consider in terms of capital. But we're comfortable with the base that we have and we don't feel that we need it at this point.

Gabriel Duchesne, National Bank Financial

Okay. Thanks for repeating that information. Again, apologies and good quarter. Thanks.

Yvan Deschamps, Executive Vice President & Chief Financial Officer

No problem. Thank you, Gabriel.

Operator

And we can now take our next question from Marcel Medina from TD Securities. Please go ahead.

Marcel Medina, TD Securities

Thank you. Most of my questions have been addressed but just on the capital one more if I could take it one step further. Is there a level of loan growth where you do start to consume that capital? Is it 70% for the overall bank or is it higher than that, or is it more complicated that you can't provide that simple of an answer?

Yvan Deschamps, Executive Vice President, Chief Financial Officer

I'm not sure about your 70%. But the key comments I could give you is that in a normal year with, for example, if we had had the growth that we expected at the beginning of the year with double-digit or so growth in commercial, with stabilization, personal and growing in 2023, with the improved profitability that we have, it also adds to the capital generation that we're having. So we do intend to put in place a plan where the internal capital generation sustains mostly that growth. But we have the catch-up to do, that catch-up happened over the last few quarters. It did reduce the capital, but for me, it's really a positive outcome of really redeploying that capital and generating profitability with it. And as I mentioned, we were at 9% pre-pandemic, so there's no stress in the CET1 with it being at 9.3% right now because we're above where we were pre-pandemic.

Marcel Medina, TD Securities

Okay. Thank you. That's it for me.

Operator

And we can now take our next question from Darko Mihelic of RBC Capital Markets. Please go ahead.

Darko Mihelic, RBC Capital Markets

Hi, thank you. I know we've gone over so thank you for taking my question. And a lot of my questions have been asked and answered so I thought maybe, Rania, I would ask you a couple of outlandish questions just to finish this off. Because I'm sitting here punching in my model, everything that you guys talked about, everything looks neat and tidy. When I look at the appendix - appendices, everything is going according to plan. And the way my mind works is when everything is going according to plan, I start to worry about what could go wrong. So my question, Rania, is what could go wrong in the second half of the year? I'm thinking about outlandish things like the French language law in Quebec, the - maybe the union coming back. Can you give me what is your biggest fear in this year of execution for the back half of the year?

Rania Llewellyn, President and Chief Executive Officer

Well, Darko, thank you for these outlandish comments at the end of the call, but delighted to answer some of them. Listen, I get paid to worry and to think about the future. And so I don't think I'd open my remarks by saying that we're confident that we're going to exceed our targets if we're not comfortable as a management team in terms of the quality of our portfolio, our underwriting capabilities, our ability to actually manage through all those volatile macro changing environments. And I think we've been delivering quarter over quarter and showcasing that. We showed that through the pandemic as well. And so I think our cautious, disciplined, prudent approach is definitely paying off. We're confident in our ability to deliver on our digital roadmap, and again, we've been delivering quarter over quarter.

The biggest thing that I always talk about is people, people, people. We're in the people business and that's really where we spend a lot of time. And that's why we've always said culture is going to be our driving force. And so ensuring that our people are equipped, we're attracting the right talent, we're retaining them, we're promoting them internally. And that's really the role of leadership and management throughout the whole organization. And that's why we increased our sales this quarter as well, so again, it really speaks to prudently managing what we think could potentially be on the horizon and how do we weather through that storm? And that's why we're also prudently managing our capital and that's why we're pausing our share buyback program. It's not that we're concerned, but it's being cautious and prudent. And so maybe I'll just leave you on that note, but we're very confident at this point that we're going to exceed our financial 2022 targets.

Darko Mihelic, RBC Capital Markets

And with respect to employees, just getting back to my concerns on costs and possibly the union coming back, is there any concern or anything - any indication out there at all that that is even plausible at this point in time?

Rania Llewellyn, President and Chief Executive Officer

So from a cost perspective, salaries have gone up and so ensuring that we retain our top talent, as we're attracting new talent, the cost of attraction has gone up, but we've been offsetting it with other things. And as I mentioned in my comments, salaries is just really one component of making sure that your employees are engaged. So as an employer, we focus on ensuring that our employees are engaged and are happy. In terms of the union, I mean, that's really between the employees and the union. So it's not something I can comment on other than we know, based on our most recent engagement with a third of our workforce. And we are doing another employee survey at the end of the year in September which is one of the key metrics, we feel that there's re-energized, they're excited about their future, they're committed about our success and so we're feeling very confident in terms of attracting and retaining talent as we stand today.

Darko Mihelic, RBC Capital Markets

Excellent. Thank you very much.

Rania Llewellyn, President and Chief Executive Officer

Thanks, Darko.

Operator

I would now like to hand the call back to Rania Llewellyn for any additional or closing remarks.

Rania Llewellyn, President and Chief Executive Officer

In closing, I am pleased with our strong results this quarter and continued momentum into Q3. We redeployed capital accumulated during the pandemic toward sustainable, profitable organic growth and internal capital generation is expected to sustain loan growth for the remainder of the year. We continue to apply strong cost discipline across the organization and identify additional cost optimization opportunities. Our credit quality is sound and we are confident in our strong underwriting practices and highly collateralized portfolio to manage through macroeconomic uncertainties.

We continue to make significant progress on our strategy. Over the second half of the year, we will be focused on initiatives that drive customer acquisition, including the rollout of our new public website with a new look and feel and enhanced and simplified user experience, additional targeted marketing, and the rollout of our new brand and refresh logo that I announced at our AGM in April. And the delivery of our digital onboarding solution and reimagined visa experience which will enable us to grow products with existing customers, acquire net new customers, and continue to grow our national presence. Our one winning team is engaged and we continue to make solid progress against this plan. We are confident in our ability to exceed our 2022 financial targets despite the uncertainties in the market. Thank you for joining the call today.

Operator

This concludes today's call. Thank you for your participation. You may now disconnect.