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Texas Capital Bancshares, Inc.

Q2 2022 Earnings Conference Call

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CORPORATE PARTICIPANTS

Rob Holmes - *President, Chief Executive Officer*

Matt Scurlock - *Chief Financial Officer*

Jocelyn Kukulka - *Director of Investor Relations*

Operator

Hello, and welcome to today's TCBI Q2 2022 Earnings Conference Call.

I would now like to hand the call over to Jocelyn Kukulka, Head of Investor Relations. The floor is yours. Please go ahead.

Jocelyn Kukulka

Good morning and thank you for joining us for TCBI's Second Quarter 2022 Earnings Conference Call.

I'm Jocelyn Kukulka, Head of Investor Relations.

Before we begin, please be aware that this call will include forward-looking statements that are based on our current expectation of future results or events. Forward-looking statements are subject to both known and unknown risks and uncertainties that could cause actual results to differ materially from these statements. Our forward-looking statements are as of the date of this call and we do not assume any obligation to update or revise them. Statements made on this call should be considered together with the cautionary statements and other information contained in today's earnings release, our most recent annual report on Form 10-K, and subsequent filings with the SEC.

We will refer to slides during today's presentation, which can be found, along with the press release, in the Investor Relations section of our website at texascapitalbank.com.

Our speakers for the call today are Rob Holmes, President and CEO, and Matt Scurlock, CFO. At the conclusion of our prepared remarks, our Operator will open up a Q&A session.

Now, I'll turn the call over to Rob for opening remarks.

Rob Holmes

Thank you for joining us today to discuss our second quarter results, which represent another important step in the transformation of our firm.

It has now been nearly 11 months since we announced our strategy on September 1st of last year, and we are taking deliberate, meaningful steps towards fulfilling our commitment to build a Texas-based, full-service financial services firm that can seamlessly serve the best clients in our markets through the entirety of their lifecycles.

We told you that delivering against this objective would require us to: reorganize the front and back of our operating model around client delivery, emphasizing client experience; aggressively realign our expenses to invest directly in expanded coverage and improve capabilities; and reposition our capital base in

support of businesses where we can be relevant to clients by offering broader product and services, not just a loan commodity. We also told you doing so would be hard, because building something of value is, but when we deliver on our strategy, we will have a business model that generates structurally higher, more sustainable earnings, and a financially resilient balance sheet geared to supporting our clients through market, as well as rate-driven cycles. To monitor our progress and hold ourselves accountable to these commitments, purpose-driven routines were established, and are maintained, in every area of the firm.

This focused approach continues to yield early results, as we add people, products and increasingly new clients at a pace consistent with our plan. Over the last year, we established foundational principles to cover markets in a smart and disciplined way, resulting in improved client engagement and sustained market share gains, which again this quarter showed up in the form of loan growth, with C&I loans increasing 34% year-over-year. Of all client relationships that were presented at Balance Sheet Committee meetings during the second quarter, we expect over 70% to do identified incremental business with us across our platform.

As we continue to grow market share, improving platform maturity will enable us to better serve the breadth of client needs, while further balancing our revenue sources. Our biweekly Balance Sheet Committee meetings are proving effective at connecting our strategy directly to our actions. Banker-led Client Teams are now appropriate involving leadership across the entire firm when looking to deliver the outcomes our clients deserve. While undoubtedly starting from a small base, this is evidenced, in part, by the 35% year-over-year growth in fee income from our three areas of focus: Treasury Solutions, Private Wealth and Investment Banking. This quarter also represents the first increase in quarterly year-over-year total revenue since the exit of the correspondent lending business in the second quarter of 2021.

Growth in Investment Banking revenue this quarter was driven primarily by swap fees and loan syndications, as late-stage pipelines referenced on our last call materialized through the quarter. Pipelines remain strong and our capital markets and loan syndication businesses should continue to gain traction and benefit from the distribution capabilities coming online this quarter and the lead left capabilities we expect to deliver this year.

Also, consistent with the timing described on the last call, we opened our sales and trading floor in May. Our trading activity for the quarter was realized in mortgage securities sales and trading, helping our clients manage pipeline and interest rate risk through TBA hedging and facilitating liquidity in specified pools. Professionals leading our mortgage whole loan and corporate loan trading desk are now on platform and we remain on track to be active in these markets this year. Excitingly, we have already seen excellent collaboration between our mortgage finance and mortgage sales and trading businesses, and we expect our Corporate Loan Team will similarly complement our existing syndicated finance business, offering our corporate and middle-market clients access to institutional capital markets from our Dallas-based trading floor.

I would like to note that the successful launch of our trading floor has not impacted our overall appetite for risk exposure. Our sales and trading activities to date have centered on facilitating transactions for our clients as riskless principal or as agent; meaning, the broker dealer has operated with zero market risk at

all times during the quarter. As we mature the business, we will remain focused on facilitating market access for our clients and managing our risk exposure within the overall tolerance of the firm. We expect to consider a thoughtful and appropriate exposure to risk, enabling our clients' success, such as in connection with a best efforts underwriting or facilitating our clients' hedging needs. We will be thoughtful and prudent about risk in providing these services to our clients. Importantly, we are still in the early stages of a multi-year journey with a platform that is just now coming together, but are encouraged by growing top line revenue resulting from emerging returns on our significant investment on expanded banking capabilities for best-in-class clients in our Texas and national markets.

During the quarter, the overall mortgage market experienced continued rate volatility, resulting in compressed profit margins and reduced cash flow for our mortgage finance clients who are transitioning to lower market volume. As a result of this expected challenging operating environment, one of the firm's mortgage warehouse clients filed for bankruptcy at quarter end, which triggered a default, the immediate downgrade to substandard for the outstanding balance of $144.6 million and the implementation of the CRT First Loss Protection. We have always viewed mortgage warehouse as a low credit risk offering with a very low realized loss given default due to the strong collateral values and inability to liquidate promptly, along with the strong protections we have in place from an underwriting perspective. This fact pattern has been proven out in the bankruptcy process as our exposure has been fully de-risked.

We received multiple bids for these granular, well underwritten mortgages, several of which were accepted, to take the market risk of our position off the table. As of today, the majority of the exposure has been liquidated and we expect the remaining trades to close in the near term with no loss to the firm or CRT investors. Our ability to act quickly, through a pre-established process, to remediate the credit exposure in less than 45 days was consistent with our expectations.

We remain committed to recycling capital and expenses by reinvesting in organic growth to achieve our vision of creating a more valuable firm for our shareholders. As we identified last year, concentrations in loan portfolio and against the capital base required rationalization. The balance sheet transformation has been in progress for 18 months, as investments to support the development of a core C&I offering have begun to right-size the business mix. The balance sheet transformation to date is following the strategy laid out last year and, as the financial results this quarter indicate, early successes are taking root.

We know that delivering shareholder returns is dependent on not only higher quality earnings, but on a lower cost of capital earned through financial resiliency. Given the rapidly evolving rate environment and the economic outlook, we continue to evaluate options to accelerate the balance sheet transformation and to insulate the firm from changing market conditions. Matt will walk you through the actions we have taken this quarter, including the firm's first interest rate cash flow hedge, which efficiently reduced asset sensitivity.

Thank you for your continued interest and support in our firm. We are excited about our accomplishments to date and the year ahead.

Now, I'll turn it over to Matt to discuss this quarter's results. Matt?

Matt Scurlock

Thanks, Rob, and good morning.

Let's begin on Slide 8.

Second quarter results depict an emerging realization of the longer-term financial outcomes associated with the significant and continued shift in allocated expense and capital to support our defined strategic objectives.

Total revenue was up $27.9 million, or 14% linked quarter, and increased $4.7 million when compared to Q2 2021, marking the first year-over-year quarterly improvement in the last year. Results were positively impacted by a $22 million increase in net interest income associated with continued core loan growth and realized benefits of our deliberate increase in asset sensitivity heading into the tightening cycle.

As Rob described, we were also pleased with early contributions from our fee-generating businesses, which should, over time, grow in scale as we improve our relevance with a now consistently expanding client base.

Non-interest expense continues to increase quarterly, as savings realized last year are redeployed into higher value initiatives that have the foundational tenets for future scale. Salaries and benefits increased again this quarter and are now up 20% year-over-year, while total non-interest expense increased only 10%, marking continued success in self-funding talent acquisition and deploying technology-enabled capabilities necessary to deliver the critical early stages of our transformation.

The velocity of change in the interest rate environment is causing tactical repositioning and we will look to pull forward portions of the transformation that are rate-dependent, or make sense, given the accelerated pace of new client acquisition.

Taken together, PPNR increased 33% linked quarter to $67.5 million, reflecting notable progress, relative to our previously published guidance of achieving year-over-year quarterly PPNR growth by late this year or early next.

Net income to common was $29.8 million for the quarter, down $5.5 million quarter-over-quarter, driven primarily by increased provision expense of $22 million, compared to a $2 million negative provision in Q1. The provision was predominantly related to $2.4 billion in quarterly loan growth.

Credit trends remain stable and, excluding the one mortgage finance credit Rob mentioned that was downgraded at quarter end, criticized loans decreased $17.1 million quarter-over-quarter to 1.91% of LHI. The rapid rise in interest rates over the quarter resulted in a decline in AOCI of $66.8 million. Further declines would be primarily driven by changes across the yield curve, mainly two-year through ten-year, and less by changes in short-term rates.

Finally, during the quarter, we repurchased $50 million of shares at a weighted average price of $53.11 per share, a discount to both Q1 and Q2 tangible book value per share.

Turning to Slide 9, ending period C&I loans increased again this quarter, up $1.5 billion, or 14%, signifying continued benefit of expanded coverage, improving calling disciplines and focused execution on our defined strategy. This observed continuation in loan growth over the past several quarters has driven C&I balances, excluding PPP, $3.2 billion, or 34%, higher year-over-year.

As discussed last quarter, the number of businesses and bankers coming online continues to expand, with each quarter marked by a maturing platform increasingly aligned on the right client selection, go-to-market strategy and available product solutions. Growth continues to come primarily from new relationships, as utilization rates moved only slightly higher in the quarter to 52% and are now in line with our pre-COVID average of low 50s.

Moving to real estate, while we expected the pace of loan payoffs in commercial real estate to remain elevated this year, we anticipated they would retreat from record levels experienced in 2021, at a minimum, allowing originations to keep pace with payoffs by mid-year. Consistent with our expectations, period end real estate balances grew again this quarter by $176 million, or 4%, and are now up in excess of $300 million year to date, reflecting modestly increasing production levels and more normalized, although again increasing, levels of payoff. Consistent with our longstanding strategy in previous quarters disclosure, new original origination volume continues to be focused on multi-family, reflecting both our deep experience in the space and preference for this property type, given observed performance through credit and interest rate cycles.

Average mortgage finance loans increased by 2% in the quarter, above the market-based guidance shared on the April earnings call. Industry originations did, in fact, contract, in line with our expectations, but a modest pickup in market share by our existing clients, coupled with elongated dwell times, led to an increase in outstanding warehouse balances, relative to market volumes. Although still strong by historical standards, near-term credit pipelines have moderated across the loan book after what was an exceptionally strong quarter. As we have said before, our strategy is focused on client selection, not timing cycles, and we would expect future growth to simply be an output of our stated strategy.

Moving to Slide 10, early on, we recognized and communicated that transitioning the funding base to our target state would be both difficult and take time, and that we would ultimately measure success by our ability to densify the balance sheet through investments in businesses where we could be relevant to our clients through multiple touchpoints, while moving away from a model reliant on a collection of separate funding sources and credit distribution channels. We noted in the last call that as rates rise, our early efforts to achieve this outcome would yield positive results, but that while both our business model and balance sheet were better positioned relative to the same point in the last tightening cycle, we are not yet at target state.

Total ending period deposits were flat quarter-over-quarter, with changes in the underlying mix reflective of a continued funding transition in a tightening rate environment. Non-interest-bearing deposits represented 49% of total deposits at period end. Quarterly average non-interest-bearing deposits were down 3% quarter-over-quarter, as a sustained market-driven contraction in mortgage finance deposits offset another quarter of growth across the rest of the Bank. Non-interest-bearing deposits in our core C&I businesses are now up 14% year-over-year, reflecting our focused strategy to generate and sustain core

operating account growth. The rapid move higher in short-term rates over the course of the last 90 days drove additional repositioning within our interest-bearing deposit base, resulting in continued de-emphasis of our highest cost, most rate-sensitive deposit sources in favor of more granular and modestly less rate-sensitive options, including Bask.

Turning to NII sensitivity, on Page 11, shown in the middle of the slide are the results of our asset sensitivity modeling, which increased again this quarter to 9.9%, or $91 million, in a plus 100-basis-point shock scenario. The core component of our asset sensitivity profile is the 82% of the total LHI portfolio, excluding MFLs, that are variable rate. Seventy percent of these loans are tied to either prime or one-month LIBOR, transitioning to BSBY or SOFR. Driving the quarterly increase in asset sensitivity was the impact of $3 billion of loans coming off floors during the quarter. At this time, there are only $600 million of loans still at their floors.

We began taking steps this quarter to reduce our asymmetric interest rate exposure and turning it into a series of cash flow hedges meant to realize the benefits of the forward curve, but, more importantly, began augmenting earnings generations should rates fall in the future. We have a variety of tools to prudently reduce this exposure, including expanding the use of fixed rate loans, managing duration in the investment portfolio, and the use of derivatives. If the current rate outlook remains intact over the quarter, we will look to more proactively use the levers at our disposal.

Moving to Slide 12, net interest margin increased by 45 basis points this quarter, while net interest income rose $22 million, predominantly as a function of increased loan volumes and higher yields, partially offset by increase in funding costs. The timing associated with the late quarter Fed moves, coupled with observed spot rates at June month end, suggests the full impact of the 2Q rate moves will be more fully realized in the third quarter.

The investment portfolio remained relatively flat quarter-over-quarter, with cash flows slowing from approximately $100 million last quarter to roughly $90 million this quarter. We purchased $260 million in new securities this quarter, primarily in two- and three-year treasuries, which are coming on the books at a roughly 3.1% yield, versus those rolling off at closer to 1.3%.

Turning to Page 13, the trends established late last year remain intact and we continue the ongoing process of systematically aligning our expense base behind our published strategic priorities. We noted on the last call that our primary objective is not absolute size, but instead productivity, and we remain focused on investing against what we believe is a significant and unique market opportunity.

Consistent with our expectations, total non-interest expense increased $11.2 million, or 7%, quarter-over-quarter and grew $15.2 million form the second quarter of last year. Importantly, salaries and benefit expense is up $17.1 million, or $2 million higher than total expenses over the same period, evidencing our success repositioning the expense base towards our stated strategy. While we are focused on the cadence of expense save redeployment and investment in the Bank, it will not be linear, and given the potential for noted acceleration of desired capability build, we are increasing the high end of our expense guidance to mid-teens.

Moving to capital, we reiterated on our last call the firmwide commitment to managing the capital base in a disciplined and analytically rigorous manner, focused on driving long-term shareholder value. We also noted that given the unique intersection of interest rate dynamics, the Bank's expected earnings profile and the current market valuation, we would evaluate the opportunity to accelerate capital return to shareholders through a tangible book value-accretive share repurchase program authorized in Q1. As Rob mentioned in his comments, that construct materialized during the quarter, resulting in us repurchasing 942,000 shares, or approximately 2% of total common shares outstanding, at a weighted average price of $53.11, which is below both Q1 and Q2 tangible book value.

CET1 and total risk-based capital finished the quarter at 10.46% and 14.42%, respectively, in line with peers, and in excess of the medium-term internal targets described last year. Our capital preference remains supporting our defined strategic goal of financial resilience, and our anticipated focus in Q3 will return to reinvesting internally generated capital into our growing franchise.

As Rob mentioned, criticized loans increased at quarter due to the default of one mortgage warehouse client. Historically, the event of default for the Bank's counterparties in this industry has been infrequent. In the unlikely event of default, we are confident in our proven structures, well prepared to respond with comparable speed, and have the expertise to do so.

We continue to proactively monitor for potential recessionary exposures caused by economic and geopolitical uncertainty. As we mentioned during our last call, credit disciplines established at the beginning of COVID, including quarterly borrower-specific reviews, quarterly portfolio reviews and client-specific strategy assessments, remain in place. Elevated awareness continues, both in monitoring the existing portfolio and ensuring our desired credit risk appetite is being consistently applied to new client acquisition.

An update to full year guidance is contained on Page 14. To both account for the velocity of change in the interest rate environment and better highlight the impact on our potential financial performance, we have updated our methodology this quarter to include the impact of forward rates.

Mortgage market expectations for the year indicate a 40% decline in originations. However, based on our experience and the additional products we can now offer our mortgage finance clients through the Investment Bank, we expect to outperform the industry with mortgage finance loans declining low 30s for the year. Given the rate environment and movement of loan rates off floors, coupled with strong core Q2 loan build, we expect total revenue to increase year-over-year in the mid to high single digit percent range. As I indicated earlier, in addition to already in-flight investments, we will also look for opportunities to pull forward expenses related to planned infrastructure build and expect full year non-interest expense growth in the low to mid double digits percent range. Together, these expectations could result in a recognition of our year-over-year quarterly PPNR growth one quarter earlier than we had previously indicated.

With that, I'll hand the call back over to Rob.

Rob Holmes

Thanks, Matt.

Operator, do you want to turn it over to questions?

Operator

Thank you. Our first question today comes from Brad Milsaps from Piper Sandler. Your line is open, please go ahead.

Brad Milsaps

Hey, good morning.

Rob Holmes

Good morning.

Matt Scurlock

Good morning, Brad.

Brad Milsaps

Rob, you mentioned in your prepared remarks that you anticipate 70% of the loans, I think, that you saw in Committee this quarter to also use other TCBI products. I was curious if you could maybe talk specifically about deposits. Is it too early to know if you're going to be able to convert a lot of those into deposit customers? I just kind of wanted to get a sense of—if you guys could talk a little bit about when, maybe, the slide in DDA might come to an end with some of the investments you've made in Treasury.

Then, as a follow-up to that, Matt, just can you talk about the difference and the betas between the indexed funding that you ran off versus the interest bearing deposits that you brought in for the quarter?

Rob Holmes

Yes, thanks for the question, it's a great question. Matt can talk about the incremental amount of investments we've made on the Treasury platform and deposit betas. What I would say is—what we said before, Brad, was this transformation is about holistic relationships based on client selection. The amount of transactions going through Balance Sheet Committee, there's about 50% of those that are new clients or prospects, new logos, if you will. I would say the vast majority of those, over 70%, have some sort of Treasury component to it, and as you know, that lags. Winning the Treasury business is about 10% of the effort, then you have to onboard them correctly, and it takes times. What I've found historically is whatever the expectation of ramp of that new Treasury business, in my prior life, you never got above 80%. Here, the good news is we are exceeding 100% of expected ramp in some cases—I think it has to do with size of wallet of this client base, etc.—and it's been primarily or virtually all domestic. So, the ramp's higher, expectations are exceeded on that end, and the ramp is realized sooner, but it still lags loan growth. Loan is typically the first thing that we onboard with a new client, but we have seen new client acquisitions without the loan product, as well.

Does that answer your question?

Brad Milsaps

Yes. Do you have a sense for maybe how large the opportunity is with those existing customers on the deposit side?

Rob Holmes

With the existing or the new, what I would say about the …

Brad Milsaps

With the new, yes, the new. Yes, the new.

Rob Holmes

Oh. It's totally dependent. So, business banking, there's one category. In middle-market, another. In corporate, yet another. So, it's totally dependent upon the segment, but it's substantial, especially given where we're starting.

Matt, do you want to talk a little bit about the—well, let me just add one more thing about that, because we talked about the Balance Sheet Committee, so let me just add with this.

We have an opportunity with our existing clients, not just the new, so of all the transactions we've looked at since we started the Balance Sheet Committee, rigor and discipline, we've only looked at about 20% of our existing portfolio. What that means is we have, like, 80% of capital that we already have committed under a different strategy without the want, desire or need, or capability to become relevant to our clients, that we get to look at. That's one of the most exciting things for me, is to go reinvest, if appropriate, $16 billion of commitments into new clients or with existing clients where new capabilities will be relevant and considered. That's just a huge opportunity.

Matt Scurlock

I think, Brad, we've been consistent in saying that a leading indicator of our ability to actually grow operating deposits is loan growth in C&I, and that we'd be willing to take tactical repositioning in the interim to support that loan growth, as long as we had confidence that our existing routines are going to result in us ultimately growing the operating deposit base.

Then, maybe just to address your question on non-interest bearing deposits directly, let me start with the component that does relate to mortgage finance. So, as you know, generally, a lot less liquidity in the system right now. One of the reasons for that is the lower refinance rates. For the portion of our non-interest bearing deposits that are escrow accounts, when a loan is refinanced, those proceeds would sit in the account until we made it to the bond investor. That volume has completely evaporated, as the economic incentive to refi has largely left.

If I move to the core commercial bank, we've nearly doubled the spend in core Treasury Solutions coverage and products since Rob's arrival, and we have over a third of our existing technology product budget that's directly against the next wave of improvements in that area. We're pleased with our current progress and pipeline in terms of growing core operating deposits, and we feel like with the established routines in place, coupled with the pace of client acquisition, that we should start to see some growth in that area in the back end of the year.

Then, to answer your next question on beta—it's a pretty good first question here, Brad—the indexed deposits, as you know, and as the name implies, they have 100% beta, and not only do they have 100% beta, but they're generally large deposits, which limits our ability to extend on the asset side of the balance sheet. So, you're largely replacing those with interest bearing deposits that are significantly more granular. They're going to have a beta between 50 and 75, depending on the source. We felt like, at this period in the tightening cycle, it was the right time for us to accelerate that repositioning. Given that some of the depositors that comprise that source are likely only going to make that transition once every cycle, it now felt like the appropriate time to grow.

Brad Milsaps

Okay, great, and just so I understand, you feel like the major slide in DDA is pretty much behind you, assuming you can kind of start—some of those products that you put in place can really start to kick in towards the end of the year.

Matt Scurlock

Yes, we said it in the commentary. The non-interest bearing deposits associated with the commercial bank are up 14% year-over-year, and we're adding C&I clients at an accelerating pace every single quarter. Each incremental C&I client lands on a platform that has better capabilities than the one that landed before. So, we feel really good. Consistent with what we've said for almost a year now, that expanded coverage, while also building new capabilities, is going to result in that deposit base that we want over time. But, just to re-emphasize, Brad, as I said directly in the comments, the deposit base is not target state today. It is going to take time for us to ultimately transition it to what we want it to be.

Rob Holmes

Let me just reiterate a little bit what Matt said. Non-interest bearing deposits and C&I business is up 14% year-over-year. Our PxV, which is the activity, price times volume, inside those operating deposits is up in the mid-low-teens. So, those businesses, that's kind of a GDP business, and so we are outpacing the market in our growth and are super-excited about that, which is directly correlated to investment and client acquisition.

Brad Milsaps

Great, thank you, guys, appreciate the color.

Matt Scurlock

Thanks, Brad.

Operator

Our next question comes from Brady Gailey from KBW. Your line is open, please go ahead.

Brady Gailey

Hey, thank you. Good morning, guys. I wanted to start with the …

Rob Holmes

Hey, Brady.

Brady Gailey

Yes, good morning. I wanted to start with the defaulted mortgage warehouse loan. I know there's no loss to Texas Capital, or it doesn't appear like there's a loss on the part of Texas Capital, but did the CRT holder experience a loss, or was just credit fully resolved without any loss to anyone?

Rob Holmes

The way the CRT is structured is that it is—you have to trigger it. CRT, as I said in my comments, immediate downgrade, immediate trigger, immediate playbook response. So, it is triggered. That does not mean that we don't have to—that we can't pay it back, and what I think you'll find—and more than highly confident you'll find, Brady—is that when this is resolved, the CRT will be paid back, and that will once again support our view that mortgage warehouse is a very, very, very low risk given default, and our subsequent cost to capital over time, when we renew the CRT, we would expect to be able to point to this example and reduce our cost to capital.

Brady Gailey

I know the mortgage market is very volatile today, just with the volatility in rates, but outside of this one relationship, do you see any other, you know, turmoil or potential bumps in some of your other mortgage warehouse clients, or is this just more of a one-off?

Rob Holmes

No, we absolutely do. I liken this to back in my last stop, when oil and gas were under severe pressure and oil services firms, you've got to have great operators that can cut costs, they understand which dollar of cost is associated, which dollar revenue, and I think you're seeing is that in the mortgage business now. So, I do think that you'll see stress by those clients, some of them. The great news is one of the levers that we talked about, when I said we had six levers in the mortgage warehouse business to pull

and make it resilient—which we have done, and we've outperformed, with the market being down over 10% more than what we are in that business—one of the levers was repositioning our client base, and we talked about client selection here all the time. We've moved upmarket and syndicated more off for the higher holds, and so we feel like we have a great handle on our exposure, even though we do feel that it is very, very low risk of loss in default.

I'll tell you another thing, too. The value of this platform really shined with this issue. What I mean by that is we have a trading desk that is very, very active in this industry, and expertise on that desk. We have mortgage warehouse professionals and teams running that, that are over the top, as well. That combined market knowledge will allow us to see around corners and outperform.

Brady Gailey

Okay, all right, that's helpful. It's nice to see you guys repurchase about 2% of the Company. I know common equity Tier 1 had a move this quarter, it's now down to 10.5%, still above your 10% target, but is it right to think about a lesser amount of share buybacks going forward, unless the stock dips well below tangible book value?

Rob Holmes

We're doing a lot of corporate finance disciplines here today that were absent before. We have a shelf in place. Matt discussed we did our first hedge. We have a share repurchase program in place. We will keep those things in place and those levers available at all times, but we would rather invest in the organic strategy that we've stated, where we can drive structurally higher returns, than repurchase shares, but I don't want to commit to not doing it, it's just not our first priority.

Brady Gailey

Yes, and then finally for me, just some more details, broadly speaking, on the cash flow hedges you all entered into. Can you just give us a sense as far as the size and some of the big picture details here?

Matt Scurlock

Yes, you bet, Brady. We did $750 million over the course of the quarter, three separate trades, two related to prime, one related to SOFR, received fixed, paid float, generally a three-year term. We said in the comments, and will reiterate now, we would anticipate continuing to be active on that over the next few quarters, of course contingent on the rate outlook. I'd say a benefit of doing it in the second quarter is that the curve gave you the opportunity to actually pull forward earnings, or said differently, realize some

of the asset sensitivity, while also building in rates fall protection. While that is certainly a nice benefit, that was not the driving factor for us. The driving factor for us of locking in hedges now is to start to neutralize some of the asset sensitivity, so we actually have, as Rob said, structurally higher, more sustainable earnings when rates do inevitably change.

Brady Gailey

Yes, that makes sense. Thanks for the color, guys.

Matt Scurlock

Yes.

Rob Holmes

Thanks.

Operator

Our next question comes from Michael Rose from Raymond James. Your line is open.

Michael Rose

Hey, good morning, and thanks for taking my questions.

Rob Holmes

Good morning, Michael.

Michael Rose

Hey, good morning. So, just looking at Slide 10, I appreciate the breakdown of the indexed deposits, if I kind of look at kind of the three buckets, defined as kind of indexed, the brokered deposits, maybe what you have from Bask, kind of where was that when you came in, Rob, where does that kind of stand now, and where do you think it'll get to? Because, it does seem like you're going to have to have longer term a little bit more elevated higher cost funding, relative to some of your peers, because the growth, given the amount of lenders that you've brought on and relationships that you're building—I know growth is the byproduct, but, nonetheless, you can see the evidence of what you guys are doing in this quarter's results. How should we think about the deposit mix, I guess, in the intermediate term as you balance growth versus profitability? Thanks.

Matt Scurlock

Hey, Michael, it's Matt, I'll take a shot at that, and Rob can certainly fill in what I've missed.

When Rob got here, we had basically a third of the funding mix sitting in institutionally indexed deposits, of which, we said pretty directly in the comments, there's legacy strategy and a series of deposit-gathering businesses that then funnel funding over to a series of loan-generating businesses with no connectivity to a common client. The go-forward strategy is the complete opposite of that, and that you want to attract a client one time and go deliver significant amount of value to them through the multiple products and services, of which the most important to us is be their core operating bank.

Over the last year, we've driven that one-third of total funding being institutionally indexed down to, end of period this quarter, under 20%. We've got a long-term target there for it to be under 15%. If you look at the deposit outflows over the last year $4.5 billion of that was FI and NBFI, or the institutionally indexed money, which is largely sort of our discretion on how we wanted to manage that. If I think through where we are today and then where we're going to go, I think the underlying moment on the core operating deposits, as we mentioned, is actually really strong, and that's certainly a byproduct of the investments that we've made, both in terms of talent and capabilities, but it's also just the result of a real organizational commitment to focus on that.

Is it going to be linear progression up from 49% end of period to hit some target? It won't be linear, unfortunately. Nothing on this balance sheet is going to be linear for a while. But, in the interim, we have multiple options that we can use to fund the right client acquisition. That is certainly a source that we like. You saw us add about $600 million in brokered CDs this quarter, equally split between three-month, six-month and 12 month. So, we feel like we've got plenty of options in the interim to continue to go bank the clients that we want and also drive the balance sheet that we're after.

Rob Holmes

Hey, Mike, just one other thing, and this might sound trite, but I just want to be clear about something that Matt said. He said we were going to transition the balance sheet from disconnected funding sources to lending sources. Prior here, we had lenders, which you referred to, that didn't understand a broad array of product and services as a large percentage of our population of bankers. Today, our business bankers understand treasury and ask for the business. Our middle-market bankers understand treasury and corporate finance, and other products and services, and our corporate bankers certainly do. So, we hope not to have any lenders on our platform, we want to have bankers that understand clients, their needs, their relationship and their different lifecycles. I know it sounds, maybe, trite, but I just want to graduate from an oversized community bank with only lenders to a full-service financial services firm with bankers that are well rounded.

Michael Rose

I appreciate the color, and maybe just one follow-up on this quarter's growth, and I'm sorry if I missed it. How much of it was actually kind of line utilization versus kind of new requests? Because, I think it's important. Line utilization has gone up for everybody, but you guys have clearly, like I said, added a bunch of lenders, I would suspect a bunch of clients, as well, as they migrate their books, and things like that, and then what was that like for this quarter, and then how should we think about that moving forward? Thanks.

Matt Scurlock

Yes, it's good question, Michael. It went up about 2%. It's now back consistent with where it was pre-COVID. The majority of the growth came from new client acquisition, which the preponderance is Texas-based C&I, which is exactly what the strategy is geared to go after.

Michael Rose

I appreciate the … (cross talking)

Rob Holmes

Hey, Michael … (cross talking)

Michael Rose

Yes?

Rob Holmes

I can't help myself. If you look at what we've done—think about a year ago, the mortgage warehouse dropping as much as it does, and if we hadn't made all the improvements to it, the gestation, TBA, and the other things, the strategic changes, it probably would have been more in line with market, so it would have been exacerbated. We outperformed in mortgage, and during that course of the year, we built a segmented bank with close to two-and-a-half times more C&I bankers, with great bankers that were on the platform, that are still here, with new bankers that joined, but we have a lot more segmented highly focused against business banking, middle-market and corporate. That bank did not exist a year ago. You had a lending platform, you didn't have the bank. We would not have been able to do that. This place would have been in a bad position had we not made so much progress over a very short amount of time with the investment in Treasury products, in Investment Banking, in Private Wealth, and the things that we're talking about. There's just such a stark contrast, that I just want to make sure people understood. Switched from mortgage warehouse reliance to strategic investment, where you can redeploy that capital at a higher profit, with more than just lending.

Michael Rose

I appreciate all the color. Thanks.

Operator

This concludes our Q&A session. I'll now hand over to Rob Holmes for final remarks.

Rob Holmes

I would just say thank you to everybody for your continued interest in the firm. Please follow up with Matt, Jocelyn or myself if you have further questions. We'll look forward to seeing you next quarter.

Operator

Today's call is now concluded. I'd like to thank you for your participation. You may now disconnect your lines.