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Texas Capital Bancshares, Inc.

Q2 2025 Earnings Conference Call

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CORPORATE PARTICIPANTS

Rob Holmes – *Chairman, President & Chief Executive Officer*

Matt Scurlock - *Chief Financial Officer*

Jocelyn Kukulka - *Head of Investor Relations & Corporate Development*

Operator

Good morning. Thank you all for attending the Texas Capital Bancshares, Inc. Q2 2025 Earnings Call.
(Operator Instructions)

I would now like to pass the conference over to your host, Jocelyn Kukulka, Head of Investor Relations at Texas Capital Bancshares. Thank you. You may proceed.

Jocelyn Kukulka

Good morning, and thank you for joining us for TCBI's Second Quarter 2025 Earnings Conference Call. I'm Jocelyn Kukulka, Head of Investor Relations.

Before we begin, please be aware this call will include forward-looking statements that are based on our current expectations 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. Today's presentation will include certain non-GAAP measures, including, but not limited to, adjusted operating metrics, adjusted earnings per share, and return on invested capital. For a reconciliation of these and other non-GAAP measures to the corresponding GAAP measures, please refer to our earnings press release and our website.

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, Chairman, President and CEO; and Matt Scurlock, CFO. At the conclusion of our prepared remarks, our operator will open up the call for Q&A.

And now I'll turn the call over to Rob for opening remarks.

Rob Holmes

Good morning.

Our strong quarterly performance is the result of continued execution on our multi-year roadmap, which is delivering structurally higher, and more sustainable earnings across a broad set of products and services, with an operating model that is only beginning to deliver on its potential for future scale.

Year-over-year quarterly earnings growth accelerated materially during the quarter, with adjusted total revenue increasing 16%, adjusted net income to common up 100%, adjusted earnings per share expanding 104%, and adjusted return on average assets of 1.02%, nearing the 1.1% goal we set out for 2025.

Our now multi-quarter trends of significant new client acquisition again resulted in targeted balance sheet expansion consistent with our strategic areas of focus. Commercial loans grew 5% linked quarter, and are up 13% year-over-year, as we continue to effectively compete for, and win, holistic client relationships, which define the Firm, and for whom we can be relevant over the duration of their personal and business life-cycles.

This growth did not come at the expense of our peer leading capital ratios, as the Firm continues to build tangible common equity to tangible assets, finishing the quarter at 10.04%, alongside tangible book value per share of \$70.14, an all-time high for the Firm.

Significant investments in building our areas of focus have and will continue to drive increasingly elevated and granular revenue contributions. Earning the right to be our client's primary operating bank remains a foundational component of our Company, with sustained success again displayed by another quarter of peer leading growth in Treasury Product fees, which increased 37% year over year to a record high for the Firm. Quarterly Treasury Product Fees have now increased 8 of the last 12 quarters demonstrating the sustainability of our trajectory, and commitment to being a premier payments Bank. Early and substantial investments in these products and services have returned the expected outcomes which, as they scale, will continue to enhance profitability.

In addition to focusing on core operating account growth, our treasury platform is also contributing to expansion in longer duration, less rate sensitive interest-bearing deposits, again evidenced this quarter by a 16 basis point increase in linked quarter net interest margin. Our unique and focused client service models continue to gain scale, making it easier for our clients to bring more of their business to us through tech-enabled connectivity and same day account opening.

Despite portions of the capital markets being essentially closed in April and early May, Investment Banking and Trading Income increased 43% quarter over quarter and 4% year over year led by a rebound in Capital Markets activity, and our steadily growing Sales & Trading platform. During the quarter we also continued our Equities buildout, further expanding our research coverage to 72 companies, adding key talent in equity capital markets, corporate access, and industry investment banking coverage, while also commencing trading operations near the end of the quarter. Our breadth of product offerings and integrated client solutions provided by industry experts aligned with client needs continues to be a competitive advantage driving pipeline growth, which will be further enhanced as these capabilities begin to scale during the second half of the year.

As we close out this quarter, I want to take a moment to reflect on how far we've come. Over the past four years, we've executed a bold and deliberate transformation reshaping our Firm into a more agile, diversified, and client-centric institution. Through purposeful actions, scaling value-accretive businesses, enhancing client journeys, and driving operational efficiency, we've built a platform that is resilient, relevant, and positioned to perform through any market or rate cycle.

This quarter's results are a testament to the strength of that platform. We have delivered solid performance across our businesses, maintained risk discipline, and continued to invest in innovation and talent, all of which engender confidence we will deliver the risk-adjusted returns consistent with our published targets.

None of this would be possible without the dedication and hard work of our employees. Their commitment, creativity, and resilience have been the driving force behind our transformation and will ensure our future successes.

Thank you again for your continued support and trust. I'll turn it over to Matt to discuss the financial results.

Matt Scurlock

Thanks, Rob, and good morning.

Starting on slide 5 –

Second quarter adjusted total revenue increased \$42.3 million or 16% relative to Q2 of last year, supported by 17% growth in net interest income and 11% growth in adjusted fee-based revenue.

Linked quarter adjusted total revenue grew by \$28.9 million, or 10% for the quarter as a \$17.4 million increase in net interest income was augmented by a \$11.5 million improvement in adjusted non-interest revenue.

Adjusted total non-interest expense decreased \$14.1 million quarter over quarter, as first quarter financials are impacted by seasonal payroll and compensation expenses, and realized structural efficiencies enabled continued repositioning of the expense base in support of defined capability build.

Taken together, year-over-year adjusted pre-provision net revenue increased 52% or \$41.4 million to \$120.5 million, a record level since the announcement of the strategic transformation.

This quarter's provision expense of \$15 million resulted from continued growth in gross LHI, \$13 million of net charge offs against previously identified problem credits, and our continued view of the uncertain macroeconomic environment, which remains decidedly more conservative than consensus expectations. The firm's allowance for credit loss increased \$2 million to \$334 million, finishing the quarter at 1.79% of LHI, when excluding the impact of mortgage finance allowance and related loan balances.

As Rob noted, adjusted net income to common was \$75.5 million, an increase of 100% compared to adjusted net income to common in Q2 of last year. This continued financial progress coupled with a consistently disciplined multi-year share repurchase approach, contributed to a 104% increase in quarterly adjusted earnings per share compared to adjusted earnings per share from a year ago.

The Firm continues to operate from a position of financial strength, with balance sheet metrics remaining exceptionally strong. Ending period cash and securities comprised 23% of total assets, as the Firm continues to onboard and expand client relationships while supporting their broad needs, which again this quarter included an increase in credit demand.

Focused routines on target client acquisition continue to deliver risk-appropriate, and return accretive, loan portfolio expansion, with ending period gross LHI balances, excluding mortgage finance, growing \$387 million or 9% annualized during the quarter.

Average commercial loan balances increased 4% or \$399 million during the quarter with broad contributions across areas of industry and geographic coverage, with ending period balances up approximately \$1.4 billion, or 13% year over year.

As expected, real estate loans declined slightly during the quarter, decreasing \$159 million, including a \$53 million reduction of previously criticized assets to the lowest levels in over two years. Despite a modest increase in clients' new business volume, should the current rate outlook hold, our expectation remains that payoffs will outpace originations over the duration of the year, causing current quarter trends to continue at a comparable pace.

As anticipated, average mortgage finance loans increased 34% linked quarter to \$5.3 billion, as seasonal homebuying activity hits its annual high during the summer months.

We remain cautious on our mortgage outlook for the remainder of 2025, with continued expectation for a 10% increase in full-year average balances predicated on a \$1.9 trillion-dollar origination market.

As Rob noted, sustained success winning high quality deposit relationships continues to allow for the select reduction of higher cost deposits where we are unable to earn an adequate return on the aggregate relationship. These trends are evidenced in part by our continued ability to effectively grow client interest bearing deposits which are up \$2.8 billion, or 19% YoY, while effectively managing deposit betas, which increased to 81% in the quarter, and maintaining decade low levels of brokered deposits.

This is also observed in the ratio of average mortgage finance deposits to average mortgage finance loans, which improved to 91% this quarter, down significantly from 120% in Q2 of last year, which is positively affecting margin while improving liquidity value. We expect this ratio to remain near 90% during the third quarter as loan volumes peak seasonally and deposit balances predictably build.

Our modeled earnings at risk were relatively flat quarter over quarter, with current and prospective balance sheet positioning continuing to reflect a business model that is intentionally more resilient to changes in market rates.

In April we took advantage of significant tariff driven rate volatility to sell \$282 million of relatively short duration AFS securities with a book yield of 3.1%, reinvesting the proceeds into securities yielding 5.4%, resulting in an approximately 4-month earnback, and improvement in rates fall protection. In addition to this small repositioning, we continue to effectively manage duration in anticipation of upcoming swap maturities, adding \$221 million of additional securities yielding 5.6%, along with \$100 million in forward starting receive fixed swaps that will become active on October 1st.

We currently have \$1.5 billion of receive fixed SOFR swaps maturing in the third quarter at a blended receive rate of 292 basis points, of which \$250 million matured earlier this month. Partially offsetting this reduction, \$300 million of previously added forward starting SOFR swaps with a blended receive rate of 388 bps become active later in the third quarter. We do still anticipate future interest rate derivative or securities actions over the course of 2025, as we look to augment potential rates fall earnings generation at materially better terms than available during our deliberate pause through the mid-part of last year.

Net interest margin expanded 16 bps this quarter, as the \$17.4 million increase in net interest income was driven by improvements in funding costs, growth in loan balances and improvement in the mortgage finance self-funding ratio, partially offset by lower cash income associated with seasonally smaller balances.

Quarterly adjusted non-interest expense decreased \$14.1 million off a seasonally elevated Q1, while year over year adjusted levels were up only \$900 thousand dollars as we continue to reposition the expense base in support of consistently defined growth initiatives in areas of focus.

The total allowance for credit loss including off balance sheet reserves increased to \$334 million, an all time high for the firm. When excluding the impact of Mortgage Finance allowance and related loan balances reserves are 1.79% of total LHI, in the top decile among the peer group, and up over \$20 million relative to Q2 of last year.

Special mention loans decreased \$144.3 million quarter over quarter while total criticized loans decreased \$222 million, or 26% year-over-year. Criticized loans to total LHI decreased to 2.66%, the lowest level since 2022, with broad based improvement across both C&I and CRE. The reserve coverage ratio remains strong at 2.9x non-accrual loans which experienced a modest increase of \$20 million this quarter to levels in line with experience over the last twelve months.

Despite continued notable portfolio improvements, we remain focused on proactively assessing the credit impact of a wide range of macroeconomic and portfolio-specific scenarios. This consistent, forward looking approach reinforces our ability to adapt to evolving credit conditions while preserving balance sheet strength and supporting long-term value creation.

Consistent with prior quarters, capital levels remain at or near the top of the industry.

Total regulatory capital remains exceptionally strong relative to both the peer group and our internally assessed risk profile. CET1 finished the quarter at 11.45%, an 18bps decline from prior quarter, as strong capital generation was offset by robust loan growth. By quarter end, approximately 30% of our mortgage finance loan portfolio had migrated to the enhanced credit structures discussed over the last few quarters, bringing the blended risk weighting to 79%. Our continued client dialogue suggests that another 10% of funded mortgage loan balances could migrate into the structure during the third quarter, further improving both our credit positioning and return on allocated capital.

We continue to deploy the capital base in a disciplined and analytically rigorous manner focused on driving long-term shareholder value. During the quarter, we repurchased approximately 318 thousand shares or 0.7% of prior quarter shares outstanding, for a total of \$21 million at a weighted average price of \$65.50 per share or 96% of prior month tangible book value per share.

Turning to our full-year outlook, we are reaffirming our revenue guidance of low double-digit percentage growth, reflecting confidence in the durability of our diversified earnings platform and ability to drive consistent client engagement across a range of market conditions.

We are decreasing our non-interest expense outlook, to mid to high single-digit percent growth from high single digits percent growth previously. This reduction is driven by sustained realization of structural efficiencies, partially offset by continued platform buildout, including non salaries and benefits related costs associated with putting new capabilities into market.

The full year provision expense outlook remains 30-35 basis points of loans held for investment, excluding mortgage finance, which should enable the preservation of industry leading coverage levels, while effectively supporting our client's growth needs.

Taken together, this outlook suggests continued earnings momentum and achievement of quarterly 1.1% ROAA in the second half of the year.

Operator – we'd now like to open the call up for questions. Thank you.

Operator

(Operator Instructions) The first question we have comes from Michael Rose with Raymond James.

Michael Rose

Matt or Rob, I just wanted to get a better view into kind of the pipeline for investment banking and trading. I know you've made a fair amount of hires here recently, and we've seen the deal activity pick up on your LinkedIn page. Just wanted to get a sense for where pipelines are and how we could expect that to trend? Then if you could dovetail that with the ongoing investments that are going to be needed to kind of support the growth of that business, I know you've launched on a couple of sectors here within research and things like that, so just trying to level-set near-term expectations.

Matt Scurlock

Yes, happy to address that, Michael. So despite the fact that capital markets were essentially closed in April and through the first part of May, investment banking and trading income did come in above the guide, which was supported by strong capital markets syndication fees and the continued growth in sales and trading.

Rob noted in his prepared remarks that the continued expansion of an integration of capabilities into our existing coverage should support pretty strong fee growth in the back part of the year. So the guide currently contemplates that total noninterest income moves to \$60 million to \$65 million in the third quarter, which will be supported by \$35 million to \$40 million in investment banking fees. That expectations for full year noninterest income will move to about \$230 million to \$240 million.

On expense side, we're proud that we continue to find select opportunities to reposition the expense base against what has long been described as areas of focus. We expect expenses are going to move to the mid- to high \$190s (million) over the next couple of quarters as sizes and benefits moves into the low to mid \$120s (million). Then other noninterest expense moves above the \$70 million number that we've cited for the last few quarters.

Both of those moves are related to the capability build-out that you described, Michael, primarily in investment banking coverage and product rollout. It's not just the comp and benefits expense, it's the technology expense, occupancy expense, and the legal necessary to put those initiatives into the market.

Rob Holmes

I would just add one thing, which would be I think it's really, really important to note how the platform, including investment banking, affects NIM as well. So there's a better client journey, better advice, better dialogue with our clients. It's a more valuable banking relationship whether they use an investment banking service or not, which makes them less demanding of rate, which obviously contributed to 42 bps improvement year-to-date in NIM, which I think is sector-leading.

Michael Rose

That's great color. I appreciate all of it. Maybe just one follow-up question. I had -- probably beating a dead horse here on the ROA, but it seems like it's clearly within striking distance. I know maybe a little bit early, but just given ongoing momentum and seasoning of investments, positive operating leverage, all of the above, I mean should we expect something higher as we contemplate next year?

Rob Holmes

Look, our aspiration is not to achieve 1.10 [ROAA] and stop. I mean, you know us pretty well Michael. That was a guidepost along the way of the transformation, and we have a long way to go, and we're super excited about it. What we're certain of is that the strategy works, the client acceptance of this strategy and our bankers is actually surprising, even to me. I'm super proud of the bankers, [and] the clients were onboarding. As we said, we want to be defined by our clients. We're proud of all of them. We've reallocated a lot of capital to get the right clients onto the platform and one to one is just a mirror stop along the way.

Operator

Your next question comes from Woody Lay with Keefe, Bruyette, & Woods.

Woody Lay

(technical difficulty) any commentary on the restructuring charges in the quarter? And as I think about the low end versus the high end of the guide, is that really a reflection of the investment banking trends over the back half of the year?

Matt Scurlock

Woody, I'm not sure if there was a beginning part of that question that we may have missed. So the first thing we heard is the restructuring charges to address that. So we continue to find opportunities to drive what we term as real structural efficiencies. We're able to take expense from what we think of as less productive sources and match it up against the fee income areas of focus that we've been describing really since 2021. So that's a trend that we hope to continue and think has become a core competency for the firm.

Can you ask the second question again?

Woody Lay

Yes. And just on the guide of sort of mid to high single digits for expense growth, the low end versus the high end, does that really come down to how investment banking fees trend in the back half of the year?

Matt Scurlock

Yes. Good question. I really like about 6% full year noninterest expense growth. I think mid to high \$190s (million) in the next two quarters supports \$240 million of fee generation as well as the outlook for full year earnings.

Woody Lay

Got it. That's helpful. Then maybe last for me on capital. And just given sort of the shift in the regulatory tone, how does it impact your view on excess capital and that CET1 target of above 11%?

Rob Holmes

Doesn't affect us whatsoever. As you know, we are super happy to have what you would call excess capital, we call a strategic advantage in the market, which allows us to onboard a record number of clients each in the last 3 years. We don't see it as anything but of a competitive advantage. We have lots of uses for it. We're great stewards of capital. As you know, we have a traditional data-driven capital allocation model, and we've proven to be good stewards of it. The regulatory outlook has no bearing.

Operator

We now have a question from Stephen Scouten with Piper Sandler.

Stephen Scouten

So revenue trends were extremely strong in the quarter, which is great. I know the guide is maybe a fairly wide band here at low double-digit percent growth. But I'm curious, what would lead you to maybe raise that guidance, given what appears to be maybe some revenue trends that are ahead of schedule or maybe what would take us to the highest end of what is low double-digit growth?

Matt Scurlock

Yes. We think at \$230 (million) of fees, so the low end of the fee guide, we've got enough NII momentum, Stephen, to move to the high end of the current guide. Maybe to walk through that a bit, as Rob alluded to, for us, NII really begins with deposit repricing, which we were clearly able to push past that 70% interest-bearing deposit beta that we targeted during the second quarter, and are now at 81% since the beginning of the easing cycle.

Rob and I both noted in our prepared remarks that we've done that while effectively growing non-brokered, non-indexed interest-bearing deposits by \$3 billion or 22% year-over-year, which, to Rob's point, we think highlights improved client relevance and a sustained value proposition.

Supporting those results, we did have CDs reprice of \$986 million of CDs that matured in the quarter at 4.75 and came back on a closer to 4.25, and we've got another [\$1.1 billion] that's going to mature this quarter, an average rate of 4.62% relative to posted rates of 4.2%. Given the balance sheet momentum and multitude of relationship touch points with those consumers, we expect majority of those CDs to be replaced at current market pricing.

We don't necessarily think that we're going to see, other than the CD repricing, additional success passing on marginal decreases in interest-bearing deposit costs up to and until the Fed moves. But we do think there's enough momentum to support an increase in net interest income of roughly \$10 million linked quarter. If you carry that out for the duration of the year, I think you could pretty easily deliver the high end of the revenue guide on \$230 (million).

Stephen Scouten

Okay. That's very helpful and specific. I appreciate that, Matt. I guess as it pertains to the mortgage finance business and expected yields, if the related deposits stay in this 90% range, would you think that the mortgage finance yields could actually continue to tick up higher as that kind of drag from the deposit weighting lessons relative to what it's been in the past?

Matt Scurlock

Yes. The guide incorporates a cut in September, which would suggest that mortgage finance yields moved out into the mid-4.30s. Absent a cut, I think you said relatively flat linked quarter.

Stephen Scouten

Okay. Great. Then maybe just lastly on the expense trends. I know last quarter, you called out about \$14 million in seasonal uptick that wouldn't repeat. But obviously didn't see seemingly relative to that delta, a lot of other growth. Was there anything that maybe surprised you guys in terms of your ability to keep expenses lower than what have been expected or anything of note in terms of larger scale savings that occurred this quarter?

Rob Holmes

No. I think we've made multiple years of investments in technology across the platform that's allowing for efficiencies and greater expense management and discipline that you will see going forward as we build the platform with the ability to scale with efficiency.

Operator

(Operator Instructions) And your next question comes from Matt Olney with Stephens Inc.

Matt Olney

Good growth on the commercial lending front. I'm curious what you saw from your commercial customer behavior from April and then of course end of June. I mean, you mentioned it was a volatile quarter from a macro perspective. So just curious, as you move through the quarter, did you see any change in behavior, change utilization from all your commercial-type customers?

Matt Scurlock

Yes. Thanks, Matt. So I think we've noted on every single call since this management team has been in place that we're trying to create what we think is a pretty unique offering to provide capital to our clients really across any continuum, which includes facilitating access to bank debt.

This quarter for us generally played out as anticipated, with continued strong client acquisition resulting in 20% annualized growth in C&I, which was partially offset by we think well telegraphed payoffs in CRE, of which about a third of that was related to criticized assets.

The pipeline suggests that those client acquisition trends should remain intact heading into the third quarter, and we haven't seen really any change in line utilization linked quarter and are down about 2% year-over-year.

Rob Holmes

I would just add to that, that I see continued growth activity in the balance sheet forum is extremely high for new clients with the demand on loans going forward on bank debt, not just other types of debt, and I think you'll see continued growth as the reinvestment and the balance sheet continues to slow.

Matt Olney

Okay. Appreciate the color on that, Rob. Then I guess going back to the mortgage finance commentary. I'm a little bit surprised you're maintaining that guidance of the 10% year-over-year growth given industry expectations a little bit softer now than a few months ago. It sounds like you could be gaining some market share. Any color you can share on that?

Matt Scurlock

We think we bank really great clients in that space, Matt, and continue to try to provide a broader set of products and services to that client base. Our expectation for the market hasn't changed since the beginning of the year. So we've got a \$1.9 trillion origination market that sits on top of 30-year fixed rate mortgages between 6.8 (percent), and 7 (percent). And if that continues, we expect 10% growth in full year average balances.

Rob Holmes

I think it's important to note also, we're not trying to gain market share in that sector. We're trying to bank the select view what we think are the best clients in that sector and no more.

Operator

(Operator Instructions) And your next question comes from Jon Arfstrom with RBC Capital Markets.

Jon Arfstrom

Just a couple of cleanups here. Matt, can you comment on a higher NPL balance, obviously not concerning, but just curious what was behind that?

Matt Scurlock

Yes, a couple of C&I credits, not industry-specific, no direct impact from tariffs. I'd say just in general, on credit, I think we're really proud of how the team continues to practically manage that portfolio. I think we would view that as a pretty underappreciated portion of the transformation. So there was a minor move up in NPAs, but the ratio is consistent with what we've seen over the last few years. We added a couple of million dollars to reserve, which nominally is now at the highest level in the firm's history.

It did result in a slight reduction in the ACL coverage ratio, but the trends to the left of NPAs are quite strong. We saw a 26% reduction in year-over-year criticized loans, a 59% reduction in year-over-year criticized loans related to commercial real estate, which are the lowest level in 2 years, and then our reserve continues to be underpinned by an economic outlook that's significantly more conservative than consensus estimates.

Rob Holmes

I would just add that I think we'll continue to perform well in credit because of our client selection as well. Our bankers do a great job at that today, which I think has manifested in the stats that Matt just relayed. We feel really good about where we are, [on] our reserve levels and the performance of the credit portfolio.

Jon Arfstrom

Okay. I'm good. Fair enough on that. Rob, where are you on in your wealth management build-out progress? It feels like maybe that's the last leg here, and just curious how you feel about that.

Rob Holmes

Yes. I feel really good about it. So -- you're right. It is the last leg. We're a little behind on that. We've spoken about it. Thanks for bringing it up. We went on to the new platform in the fourth quarter of last year. That's a dramatically improved client journey. If you look at our allocated portfolios that we put our clients in, we perform as well or better than other wealth managers. So it's not the performance of that. It's more the client journey and then getting the team on the field, if you will.

We think coupled with all the new client onboardings that we've had across the commercial space and investment banking, our ability and our TAM in that space is really unbelievable. I think you'll see great growth in that in the coming quarters and years. That's a slow growth business, as you know, but it's highly durable, and we're really excited about it. I think you're about to see the first legs of it.

Operator

I can confirm we have no further questions. So I would like to hand it back to Rob Holmes for final closing comments.

Rob Holmes

Thanks everybody for your interest in the firm, and we look forward to speaking to you next quarter.

Operator

Thank you all for dialing in and I can confirm, that does conclude today's conference call with Texas Capital Bancshares. You may now disconnect. Thank you all for your participation. And please enjoy the rest of your day.