Byline Bancorp, Inc.

Fourth Quarter 2018 Earnings Conference Call

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CORPORATE PARTICIPANTS

Alberto Paracchini – *President and Chief Executive Officer*

Lindsay Corby – *Chief Financial Officer*

Timothy Hadro – *Chief Credit Officer*

Allyson Pooley – *Senior Vice President, Financial Profiles*

PRESENTATION

Operator
Good morning and welcome to the Byline Bancorp Fourth Quarter 2018 Earnings Conference Call. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star (*) key followed by zero (0). After today's presentation, there will be an opportunity to ask questions. To ask a question you may press star (*) then one (1) on your telephone keypad. To withdraw your question, please press star (*) then two (2). Please note this event is being recorded.

I would now like to turn the conference over to Allyson Pooley of Financial Profiles. Please go ahead.

Allyson Pooley
Thank you, Laura. Good morning everyone and thank you for joining us today for the Byline Bancorp fourth quarter 2018 earnings call. We will be using a slide presentation as part of our discussion this morning. Please visit the Events and Presentations page of Byline's Investor Relations website for access to the presentation. Before we begin, I'd like to remind you that this call contains forward-looking statements with respect to the future performance and financial conditions of Byline Bancorp that involve risks and uncertainties. Various factors could cause actual results to be materially different from any future results expressed or implied by such forward-looking statements. These factors are discussed in the Company's SEC filings, which are available on the Company's Web site. The Company disclaims any obligation to update any forward-looking statements made during the call. Management may refer to non-GAAP measures, which are intended to supplement, but not substitute, for the most directly comparable GAAP measures. The press release available on the website contains the financial and other quantitative information to be discussed today as well as a reconciliation of the GAAP to non-GAAP measures.

And with that, I'd like to turn the call over Alberto Paracchini, President and CEO.

Alberto Paracchini
Thank you, Allyson. Good morning, Happy New Year, and welcome to our fourth quarter earnings call. As usual, joining me today are Lindsay Corby, our CFO; and Tim Hadro, our Chief Credit Officer. I'll begin with an overview of our performance and key highlights for the quarter then pass the call over to Lindsay, who will give you a detailed overview of our financials. After that, I'll come back and give you closing remarks before opening the call for questions.

Moving over to Slide 3 on our deck. We ended 2018 with very strong quarter where we had our highest level of earnings since becoming a public company in 2017. The increase in our earnings power reflects solid execution on our organic growth strategies as well as the continued benefits from our acquisition of First Evanston. Net income came in at $17.1 million or $0.46 per diluted share, which included an asset impairment charge, certain merger-related, and conversion expenses that impacted our earnings by $0.03 per share. Along with our growth in earnings, we saw a steady increase in our level of returns. ROA came in at 139 basis points and ROTC was 15.49%. Pre-tax pre-provision ROA was 2.23% in the fourth quarter, an increase from 2.13% last quarter and 1.73% from the year ago period. The higher level of earnings was primarily driven by an increase in revenue, which came in at $67.8 million or 6.4% higher than last quarter. Our net interest income was up 1.3% with solid growth and average loan balances, offset by a decline in accretion income this quarter. However, if we exclude accretion income, the core margin expanded nicely, which increased 14 basis points to 4.13%. The quarter was strong in terms non-interest income growth, which was up 30% from the prior quarter. Our small business capital group had a good quarter of loan production, which resulted in higher gain on loan sales.

Overall, business development activity was solid with loan originations coming in at $164.9 million, which was anticipated after the very strong levels we experienced in the third quarter. Payoff activity increased, however, which moderated the net growth in the portfolio this quarter. Loans grew by $45.8 million or 5.3% annualized. The loan growth was strongest in the C&I category. Commercial banking team had a particularly good quarter of production, and we're pleased with the synergies that we're seeing from our combination. Customer activity in commercial banking was very good during the quarter and the second half of the year. We're seeing customers investing in their business, buying equipment, and expanding or modernizing facilities.

Moving over to liabilities, total deposits were essentially flat, growing by $9 million. That said, we had solid inflows of non-interest bearing demand deposits in the quarter, which increased to 31.8% of our total deposit. This allowed us to be proactive with deposit pricing, given the shift in expectations regarding additional rate increases. We've been very pleased with the deposit trends that we have seen in the Evanston market. It's customary to see some runoff after an acquisition, but deposits at the former First Evanston branches were higher at the end of the year than they were at the time of the merger. We think this speaks to the quality of the deposit base acquired, the continuity and strength of the team, and the approach taken with our integration and customer transition plans. We've also had a positive shift in the mix of those deposits as we've replaced higher-cost municipal deposits with lower-cost commercial deposits in the market.

With respect to expenses and efficiency, we continue to make strides towards our objectives in this area. Last quarter, our adjusted efficiency ratio improved to just under 55%. On a year-over-year basis, we improved by approximately 8 percentage points and our average deposits per branch increased to $63.6 million from $43.6 million, which reflects both positive impact of the transaction and the efficiencies generated from our branch rationalization efforts. Asset quality improved, with NPLs coming down, charge-offs remaining stable, and the allowance for loan losses increasing to support loan growth.

Before I pass the call over to Lindsay, I would like to take a moment to talk about the impact that the government shutdown is having on our government-guaranteed lending business. First off, I'll start by saying that we hope our leaders can come together and solve a problem directly impacting over 800,000 employees and a significant number of small businesses throughout the country. The shutdown impacts us primarily in two ways. First, it impacts our ability to obtain guarantees on new originations. In anticipation of the shutdown, we secured guarantees on loans we had in our pipeline but have not been able to secure guarantees for newer underwritings. Second, the shutdown also impacts our ability to sell loans in the secondary market as the SBA plays a role in the sale process, and their inability to participate negatively impact secondary market sales. We have experienced and navigated through shutdowns before and continue to originate new business and closed loans with guarantees. We have the financial strength and capacity to use our balance sheet and portfolio loans until the secondary market comes back to normal. More importantly, we'll continue to provide small businesses with access to capital and look forward to the resolution of the shutdown.

And with that, I'll pass the call over to Lindsay.

Lindsay Corby
Thanks, Alberto. Good morning everyone. I will start on Slide 4 with a review of our loan and lease portfolio. Our total loans and leases held for investment were $3.5 billion at December 31st, a net increase of $45.8 million from the end of the prior quarter. Our originated loan portfolio increased approximately $172 million net. This increase was offset by a decline of $126 million in our acquired portfolio. As Alberto mentioned, our payoffs were higher in the fourth quarter as we anticipated, with approximately $111 million in payoffs compared to $99 million in the prior quarter.

Moving on to deposits. On Slide 5, our total deposits increased $9 million to $3.75 billion at December 31st. We saw the strongest growth in our non-interest bearing demand deposits and our time deposits. This was offset by declines in other deposit categories. The increase in our non-interest bearing demand deposits was driven by seasonal inflows from commercial relationships, which pushed up our average non-interest bearing deposits by $18 million in the quarter. During the quarter, we were able to manage the time deposit costs, which helped us to reduce the increase in our cost of interest bearing deposits compared with the two prior quarters. Moving to Slide 6, I'll discuss our net interest income and margin. Our net interest income increased by approximately $700,000 due to higher balances of loans and leases. Accretion income decreased by $1.9 million from the prior quarter. Yield on earning assets expanded 5 basis points from 5.49% to 5.54%, which was offset by an 11 basis-point increase in our cost of deposits, resulting in a 4 basis-point decline in our reported net interest margin, from 4.73 to 4.69. When the impact of the accretion income is excluded, our net interest margin increased 14 basis points to 4.13%, primarily due to the positive impact of loan repricing and higher rates on our new loan production. Yields on loans and leases excluding the accretion income expanded to 5.75 from 5.48 the previous quarter.

Turning to non-interest income on Slide 7. Compared to the prior quarter, our non-interest income increased by $3.4 million. This was primarily due to a $4.3 million increase in our net gains on government-guaranteed loan sales. This was the result of higher volumes of loans sold, as well as a slight increase in average premiums due to a more favorable mix of loans sold during the quarter. The higher interest rate environment continues to drive increased prepayments fees that are reducing the value of our servicing assets. In the fourth quarter earnings release, we expanded our disclosures around the net servicing fee income to break out the loan servicing revenue and the revaluation of the servicing assets to provide better visibility. During the fourth quarter, we recorded a $2.9 million fair value adjustment to reflect the revaluation of our servicing assets, which once again reduced our net servicing fees this quarter. The loan servicing revenue was $2.7 million for the quarter, up slightly from $2.6 million in the prior quarter. The remaining fee income line items remain stable for the quarter, including our wealth management and trust business, with $679,000 of revenues during the quarter.

Moving to Slide 8, let's look at our non-interest expense. Our fourth quarter expenses include $1.3 million related to the significant items. Excluding these items, our non-interest expense increased 4.4%, primarily due to higher loan and lease-related expenses, occupancy expense, and professional fees. Our largest expense line item, salary and employee benefits, was relatively flat with the prior quarter. We expect to see the remaining cost savings projected for the first Evanston transaction in the second half of the year. That being said, we continue to see the beneficial impact of the acquisition on our adjusted efficiency ratio, which improved to 54.95% in the fourth quarter. Turning to Slide 9, we'll take a look at asset quality. We saw positive trends in the loan portfolio this quarter, and it remains well controlled. Our non-performing assets declined to 67 basis points of total assets from 71 basis points at the end of the prior quarter. Although we had some influence to OREO, this was more than offset by a decline in our non-performing loans and leases, largely related to government-guaranteed collections from the SBA on non-performing government-guaranteed loans. As a result, the government-guaranteed balances in our non-performing assets declined to $4.6 million from $7.3 million at the end of the prior quarter. Excluding government-guaranteed NPAs, our non-performing loans to total loans ratio remained unchanged at 66 basis points. Our net charge-offs were $2.1 million or 24 basis points of average loans and leases for the quarter, essentially equivalent to the prior quarter. Charge-offs were primarily related to the unguaranteed portion of SBA loans.

Provision expense for the fourth quarter was $3.9 million. Fourth quarter provision included allocations of $2.5 million for originated loans and leases and $1.6 million for acquired non-impaired loans. Relative to the prior quarter, our provision expense declined due to a reduction in specific impairment in the unguaranteed portion of the government-guaranteed portfolio. Our provision for the fourth quarter increased our allowance for loan and lease losses to 72 basis points of total loans and leases from 68 basis points at the end of the prior quarter, and our coverage of NPLs excluding the government-guaranteed portion increased 7 basis points to 109 basis points from the prior quarter. In addition to the traditional allowances of percentage of loan and lease metrics, we also analyze the allowance in conjunction with the acquisition accounting adjustments impacting our acquired portfolio. At December 31st, the acquisition accounting adjustments plus the allowance for loan and lease losses represented 169 basis points of total loans and leases.

With that, I'd like to pass the call back to Alberto.

Alberto Paracchini
Thank you, Lindsay. Before opening the call to questions, I want to spend a few minutes talking about our outlook and strategic priorities for 2019. With respect to our Oak Park River Forest acquisition, we have received all required regulatory approvals. We've also submitted our registration statement to the SEC but are subject to some degree of timing uncertainty there due to the government shutdown. As a result, we are unable to provide you with a target closing date at this point. Notwithstanding, we continue to move forward on our integration plans and still expect the closing to occur in the second quarter. With each acquisition we do, our integration process gets better, and we're well on our way with our Oak Park transaction. As was the case with First Evanston, we're partnering with a quality institution and team. We're excited about getting to work with our colleagues there and growing our business in the Oak Park and River Forest markets.

As far as organic growth is concerned, we expect to continue to generate solid loan growth consistent with our guidance in the mid-to-high single-digit range. We're well positioned to capitalize on opportunities in the market stemming from any dislocation, both in terms of customers and talent. We've built a solid platform. We'll continue to invest in it and have a unique position in the market. With respect to the process, we remain focused on executing our relationship banking strategy and identifying opportunities in select customer segments that we can grow. We also remain on the lookout for opportunities to do smart transactions that allows us to add core deposits to the franchise. Lastly, we'll continue to look for ways to gain efficiencies both on the revenue and expense side in order to increase our ability to invest in the business and gain operating leverage. As we start 2019, we have flexibility to support growth, take advantage of opportunities in the market, and continue to increase franchise value.

With that, operator, we can open the call for questions.

QUESTIONS AND ANSWERS

Operator
Thank you. At this time if you would like to ask a question, you may press star (*) then one (1) on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star (*) then two (2). And our first question will come from Terry McEvoy of Stephens.

Terry McEvoy
Good morning, everyone.

Alberto Paracchini
Good morning, Terry.

Lindsay Corby
Good morning, Terry.

Terry McEvoy
If I think about the first quarter outflow of non-interest bearing deposits, which had a nice increase in the fourth quarter, combined with just the impact of the recent Fed rate hike in December, could you just talk about anticipated funding costs or deposit costs in the first quarter? And then generally speaking, your thoughts on the core margin?

Lindsay Corby
Sure, Terry, good morning. In terms of where we think things are going for the cost of deposits, I think there is obviously pressure out there in the market. I do believe that with the current market outlook for the Fed hiking rates being more muted now, I do think that you're seeing some stabilization there. You're continuing to see pressure on the time deposits and the money markets, so I do think that you'll continue to see competition there and that'll cause a slight increase in terms of deposit costs going forward. Related to your question about the commercial deposits and the inflows, that’s typical again with our acquisition from First Evanston. They have larger commercial deposits that do tend to have these fluctuations from time to time, and you will see that coming through. We continue to capitalize on their commercial banking relationships that they've had and new ones that we're bringing into the bank. So, we were really pleased with the non-interest bearing performance during the quarter.

In terms of the outlook on the core margin, we are consistent in terms of what we've been guiding you to. We do think that you'll see some benefit during the first quarter from the December rate increase, though you may be a slight expansion in the first quarter but relatively flat throughout the remainder of the year.

Terry McEvoy
Great. And, then just as a follow up, given all the focus on leverage lending over last month, I remember when you went public there was mention of a sponsored finance group that you started that had a portfolio of about $125 million. And, I guess my question is how much of that would be considered leverage loans? Has that portfolio grown in the last couple years? And, just any comments about the credit health specifically of that portfolio?

Alberto Paracchini

Sure. So, the portfolio size of that segment, I guess, or that part of our commercial portfolio, Terry, is just under, just around $230 million plus or minus a couple million bucks. I think as far as credit quality and performance, it's been very, very good. We don't see at this point in time any deterioration in that portfolio. The portfolio continues to perform well. One thing to note is despite the talk in the markets about loosening of standards, covenants, structure, pricing, we're in a segment of the market that is not, we're, tend to finance lower middle market companies being purchased obviously by sponsors, but we remain disciplined in terms of both pricing and structure. So, I think the key thing for us there is to continue to see good transaction flow and just maintain our sell activity as we continue to grow in that business, but so far so good. Tim has some additional comments.

Tim Hadro
I would just like to add that the one impact we have seen from changes in the marketplace is that our hit ratio has gone down. For every ten credits we look at, we are now successfully hitting and winning fewer credits than we were in the last several years.

Alberto Paracchini
Yeah, and I think just to expand just briefly on that, I think we're very comfortable with that. Again, the key thing for us is just making sure that we continue to see good transaction flow, stay disciplined with our credit box and our model, and if our hit rate goes down, so be it. But, as long as we continue to get the at-bats, I think we'll be fine in that business.

Terry McEvoy
Thank you.

Operator
The next question comes from Michael Perito of KBW.

Michael Perito
Good morning.

Alberto Paracchini
Good morning, Mike.

Michael Perito
A couple questions. I want to start, I was hoping maybe we could spend a minute on the SBA side of the business and the government slowdown. I was wonder can you give us a little bit more color about what type of production you guys are anticipating. Obviously, the fourth quarter seemed pretty strong and I know it can be choppy even without the government shutdown. So, I was wondering, I guess number one, on that piece, and then on the other piece, if there's any other expected flow-through to the provision or expense line that that could also have an impact on?

Alberto Paracchini
I think more generally in terms of the shutdown there, I think, Mike, as we said during our remarks, we have gone through these periods before. Our team there has experienced shutdowns. We anticipated that there would be a shutdown. And, I think with respect to loans that we have in the pipeline where we were able to pull guarantees prior to the SBA shutting its doors, we continue to do business as usual. We'll close those loans. Obviously, we can't sell them until the shutdown is over, because the SBA is part of the sales process. And, with them being kind of out of the picture at this point, the secondary market is not operating normally.

That being said, we have the capacity to hold loans until the market resumes. So, I think that's just an issue of timing there in terms of waiting for the shutdown to end. As far as new business is concerned, and this is business where we didn't have the business in the pipeline prior to the shutdown beginning, obviously, we can only go so far there in terms of -- at some point we need get, we need to pull guarantees. And therefore, we're not going to be able to close new originations until the shutdown ends.

We obviously hope, we have no, wish we had a crystal ball and we could tell you the shutdown is going to end soon. But, eventually the shutdown will end and I think business will resume. We'll be able to resume selling loans in the secondary market, full guarantees on loans that we have in the pipeline, and move forward. At this point, you asked question a little bit about credit quality there, obviously, when we're trying to, as you know, we have these loans in our non-performing category where we have guaranteed portions where we want to collect on the guaranty. Obviously, timing there could be impacted, because we're not able to collect on a guarantee from the SBA until the shutdown ends. But, aside from that, we continue to operate the business. We're in this business for the long run. We have a good platform, and we'll continue to support small businesses going forward.

Michael Perito
Maybe I'll ask question a little bit differently, and you could disregard this first number – I'm just using it as an example. But, let's say we were expecting you do $31 million of revenue in the SBA business in 2019. Does the shutdown alter potentially that number, or does it just alter the timing of which that number will be recognized potentially over the course of the year?

Alberto Paracchini
I think the further – we've discussed this a lot internally. And, obviously some of it is just an element of timing. The longer the shutdown goes, the more that timing will impact call it the calendar year, so to speak, because things will slide. The flip side of that, which is I think the other part of your question is, the longer the shutdown goes, obviously, more small businesses are going to be impacted that depend on SBA financing. I don't think, or at least for our view is that doesn't mean that the demand goes away. So, we tend to view it as more of a timing issue really impacting both sides.

Michael Perito
Okay. Helpful, Alberto. Thanks for the color there. And, then maybe switching over to the expenses, just kind of curious, Lindsay, maybe if you have any initial thoughts as you start to budget for next year. I mean, I think if you adjust for some of the noise in the fourth quarter, it was a little over $39 million was the quarterly expense run rate. And, it sounds like there's still, while maybe nothing really major, still some efficiency focus that you guys are doing. So I mean, how should we be thinking about the expense build for next year as you guys obviously continue to target having the growth posture?

Lindsay Corby
Yeah, I think you're really starting to see some efficiencies come through. Obviously, based on our results this quarter you can see improvements just in terms of efficiency ratio and non-interest expenses extend to the average assets. Things are coming through slowly but surely here. And, I do think that they'll remain elevated here for the first half of the year and then come down consistent with the guidance that we've given in the past, Mike, in terms of the acquisition and we remain on track. And, I feel comfortable with where we're heading. So, there is always seasonality to do just in our core numbers, excluding the acquisition, because of the first quarter you have higher payroll taxes. We have negative 5 degrees and snow here in Chicago. So,

there's always some seasonality here in this first quarter. So, I think from a run rate standpoint, they will remain elevated for the first half and then you'll see the rest it come through.

Michael Perito
Okay. And, then just lastly, if I could quickly just on the state of the Chicago market, just curious if you've started to notice any form of accelerated disruption or anything of note over the -- as people approached year end here, and I assume there are starting to be some more year-end conversations with some of your competitors that could be involved in M&A transactions, et cetera. I was just curious, Alberto, if you can just give us a quick update on what you're seeing in the market?

Alberto Paracchini
Yeah, I think things slowed down on the M&A side, I think, with equity markets, with the performance of the equity markets in December. I think, you know, conversations that were ongoing and chatter, so to speak that was out there in the market, I think, got muted for a period of time. I think markets have come back a bit. So, I don't know -- I think it's too early to tell in terms of the level of activity that I think we can expect this year. But, certainly with valuations kind of where they are, I think it goes without saying that that's going to have some degree on impact on transactions. That being said for us, look, we have very good flexibility at this point where profitability is up. We're generating capital, which gives us a lot of flexibility to grow organically, to take advantage of opportunities, be it teams, be it obviously customers that that are impacted here a bit by the disruption in the market. And, as we said in our comments to do smart transactions like we've done in the past, we're looking -- we can look to first and foremost to look for opportunities to acquire core deposits. And, I think we remain focus on that. And, if history is a guide there, I think we'll be our share of opportunities.

Michael Perito
Great. Thank you for taking my questions this morning. I appreciate it.

Alberto Paracchini
Thank you, Mike.

Lindsay Corby
Thanks, Mike.

Operator
The next question comes from Nathan Race of Piper Jaffray.

Nathan Race
Hey, everyone. Good morning.

Alberto Paracchini
Good morning, Nate.

Lindsay Corby
Hey, Nate.

Nathan Race
Lindsay, just going back to your comments around the loan yield expansion this quarter and kind of your outlook there. I'm just curious, you know, given the prepayments that you guys had late in the quarter and so forth on the commercial real estate side of things if there are prepay

fees that may have impacted the loan yields here in 4Q?

Lindsay Corby
Yeah, that's a great question, Nate. No, it's pretty clean this quarter. There wasn't a lot in there that really stood out in terms of anything that would have accelerated, it was just blocking and tackling good new production, and we're seeing the impact of the rate environment.

Nathan Race
Okay, got it. Perfect. And, then just kind of thinking about accretion in 2019, I know it can be tough to predict and there was a decent stepdown versus what we had last quarter. I know the impact of OPRS probably in 2Q will have some impact as well. I was just curious kind of what you guys have budgeted or how we should think about the progression of accretion income in 2019?

Lindsay Corby
Yeah, and like you stated, accretion is one of those things where it's a point in time and subject to fluctuations. But, I did guide you guys down in terms of accretion levels. And, as I stated, it's hard to give you an exact number. But, I think you saw the variance between Q3 and Q4 to be around $2 million, let's call it. So, I think if you use that as sort of a guide, if you will, it would probably be pretty good.

Nathan Race
Okay. Got it. And, then just kind of last question on loan growth expectations on an organic basis, it sounds like you guys still are looking at a good amount of opportunities in the pipeline, still pretty full heading into this year. So, just curious if high single digits is still kind of a reasonable expectation on an organic basis for this year?

Alberto Paracchini
Yeah, I think, Nate, like we've stated before, mid-to-high single digits is kind of what we're operating under. Obviously, payoff activity and some things that we really have no visibility on is really the key variable there. But, in the mid-to-high single digits it's still -- we're still comfortable with that guidance.

Nathan Race
Okay, great. Thank you for taking the questions.

Lindsay Corby
Thanks.

Alberto Paracchini
Thanks, Nate.

Operator
The next question will come from Andrew Liesch of Sandler O'Neill.

Andrew Liesch
Good morning, everyone.

Alberto Paracchini
Good morning, Andrew.

Andrew Liesch
Just a question on the increase on the gain on sale premium this quarter, you referenced in the release and in the presentation it was probably due to mix shift. What was this mix shift?

Lindsay Corby
Sure. The mix shift was primarily USDA loans. So, Andrew, when you sell a USDA loan; number one, you don't share any of the premium with the government, so it's all ours; and then number two, the premiums tend to be higher given the fact that there are prepayment penalties with USDA loans. So, the premiums on those tend to trend higher.

Andrew Liesch
Gotcha. Okay. Thank you for that point of clarification. And, then my other question just revolves around the C&I growth this quarter, it's certainly impressive. I'm just curious what's driving that? Is it, are you taking market share from other players? Is it business expansion from existing customers? It was solid. I'd just like to know what's driving it.

Alberto Paracchini
I think you answered it, Andrew. I think it's a combination of both and the fact that we have our combined team now, so we took what was formerly the First Evanston team and now is the Byline team with ours. They're operating, we've integrated that. They're operating as a unit, focused on looking at opportunities and taking care of customers. But, I think you answered the question by the two statements that you said. It's a function of we're seeing customers certainly look for expansion opportunities in terms of whether it be equipment, whether it be expanding facilities, whether it be, you know, we're seeing some of that with existing customers and I think we're seeing also opportunity to take share in the market as well.

Andrew Liesch
Okay. Do these commercial customers, the new ones anyway, come with deposit relationships?

Alberto Paracchini
Yes sir.

Andrew Liesch
So would that be a source of non-interest bearing account growth?

Alberto Paracchini
Yep. And, I think in – that's, in reference to my remarks, as far as deposits is concerned, that is correct and that is our relationship banking strategy there.

Andrew Liesch
Okay, great. Thanks. That covers everything.

Alberto Paracchini
Sure. Thank you.

Operator
Again, if you would like to ask a question please press star (*) then one (1) at this time. Our next question will come from Sean Tobin of FIG Partners.

Sean Tobin

Good morning, everyone. Nice quarter.

Alberto Paracchini
Thank you, Sean, thank you.

Lindsay Corby
Thanks, Sean.

Sean Tobin
I guess just starting on the provision. The provision has bounced around due to the government-guaranteed portfolio. Can you give us any color on how to think of the reserve in the next couple quarters or even the next year?

Lindsay Corby
Sure. In terms of the provision for this quarter, it was around $4 million, which was lower than the previous quarter and was a reflection of the improvement in terms of the non-performing loans coming down and just some improvements in terms of some credits on the SBA side. So, I think on a go-forward basis, you'll continue to see consistent inflow and outflow from the SBA business. And, so we'll continue to provision accordingly under GAAP for that and continue to see our reserves grow in proportion to our loan portfolio. So, the bulk of the provision has really been coming from the growth that we've been experiencing. So, I think you'll see consistent trends in regards to that. Tim, I don't know if you have anything to add.

Tim Hadro
Yeah, I would add to that that the, in any given quarter, the amount of provision we take is, as Lindsay said, largely from new originations. But, it depends on what sector of our lending operations is doing particularly well that quarter, because we assess different loss factors based on the type of lending it is. General C&I lending is, we have certain factors. And, some of the, what I'd characterize is perhaps higher risk, higher return, we use higher loss factors. So, it really depends on the mix of business we do during the quarter.

Sean Tobin
Understood, understood. That’s very helpful. And, then I guess switching to fees. We saw servicing fees kind of jump around quite a bit in 2018. How should we think about that going into next year?

Alberto Paracchini
I think, before I pass this question on to Lindsay, one thing to note there is, because we've seen it in some of the releases from some other institutions is, so this year, in this quarter, so you saw the fair value charge or cost that is embedded in our numbers related to the servicing asset that we have for the SBA guaranteed business. I think as for the first time we're starting to provide you with more detail so that you can see the break-up between what is fair value adjustments that we're making to the asset itself vis-à-vis the underlying trend of servicing income coming in. So, I think hopefully that's more color for you guys and that gives you a little bit more clarity there in terms of what's driving that particular line.

Lindsay Corby
Yeah, so I think Alberto is spot on and that's why we broke it out. And, going forward, I think what's really been driving that volatility was that the prepayment fees, the increase here in the second half of the year. And, so will those slow down? Time will tell. We think so, but we don't have a crystal ball here. So, that's what drove it historically, and we'll see what happens next

year.

Sean Tobin
Awesome. Thanks. Thanks a lot for taking my questions. Nice quarter.

Alberto Paracchini
Thank you, Sean.

Lindsay Corby
Thanks, Sean.

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

CONCLUSION

Alberto Paracchini
Great. Thank you, Operator. So, first I'd like to thank you for joining us today. Thank you for your interest in Byline, and we look forward to speaking to you again next quarter. Thank you.

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