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PRESENTATION

Operator

Good day, and welcome to the BancorpSouth's Q2 2018 Earnings and Webcast Conference Call. (Operator Instructions) Please note, this event is being recorded. I would now like to turn the conference over to Will Fisackerly. Please go ahead.

Will Fisackerly *- BancorpSouth Bank - Senior VP & Director of Corporate Finance*

Good morning, and thank you for being with us. I will begin by introducing the members of the senior management team participating today. We have Chairman and Chief Executive Officer, Dan Rollins; President and Chief Operating Officer, Chris Bagley, and Senior Executive Vice President and Chief Financial Officer, John Copeland.

Before the discussion begins, I will remind you of certain forward-looking statements that may be made regarding the company's future results or financial performance. Actual results could differ materially from those indicated in these forward-looking statements due to a variety of factors and/or risks. Information concerning certain of these factors can be found in BancorpSouth's 2017 annual report on Form 10-K. Also during the call, certain non-GAAP financial measures may be discussed regarding the company's performance. If so, you can find a reconciliation of these measures in the company's second quarter 2018 earnings release. Our speakers will be referring to prepared slides during the discussion. You can find the slides by going to bancorpsouth.com and clicking on our Investor Relations page, where you'll find them on the link to our webcast or where you can view them at the exhibit to the 8-K that we filed yesterday afternoon.

And now, I'll turn to Dan Rollins, for his comments on our financial results.

James D. Rollins *- BancorpSouth Bank - Chairman, CEO & Director*

Thank you, Will. Good morning. Thank you for joining us today for BancorpSouth's second quarter 2018 conference call. I will begin by making a few brief comments regarding the highlights of the second quarter. John will discuss the financial results and Chris will provide more color on our business development activities. After we conclude our prepared comments, our executive management team will be happy to answer questions.

Let's turn to the slide presentation and discuss our second quarter results.

Slide 2 contains our customary safe harbor statement with respect to certain forward-looking information in the presentation.

Slide 3 covers the financial highlights for the second quarter, which was the second consecutive quarter, for which we reported record earnings. We reported record net income for the quarter of $54 million or $0.55 per diluted share. On a per share basis, this represents an increase of 34%, compared to the second quarter of 2017. Our earnings growth represents continued improvement in several fundamental items, including net income growth -- excuse me, net loan growth and margin improvement, combined with stability in our credit quality indicators and our expense base.

Reported GAAP earnings for the quarter were impacted by 2 nonoperating items, including merger-related expenses of $1.9 million as well as a small negative pretax mortgage servicing rights valuation adjustment of $0.2 million. Accordingly, our net operating income, excluding MSR, was $55.6 million or $0.56 per diluted share. On a per share basis, this represents an increase of 4% over the first quarter of this year and an increase of 33% over the second quarter of 2017. We reported end-of-period net loan growth of $121.3 million for the quarter or approximately 4% annualized. We are pleased to have this level of growth, particularly in light of the competitive pressures and the anticipated runoff we experienced in our acquired loan balances, as we worked through the integrations of our 2 merger partners. As anticipated, we experienced a seasonal decline in deposits for the quarter, following elevated first quarter deposit activity. Chris will discuss loan and deposit activity further in a moment, including some geographical commentary on our markets.

I'm also pleased to report continued upward movement in our net interest margin. Our core margin, which excludes accretable yield, was 3.63% for the quarter, compared to 3.60% for the first quarter of 2018. We continue to benefit from the upward repricing of our loans and securities portfolios. John will go into further detail in a moment.

Finally, the last two bullets on this slide relate to capital deployment. We were active in our share repurchase program during the quarter, repurchasing over 785,000 shares of our common stock at a weighted average price of $31.39. We now have approximately 3.1 million shares remaining in our current authorization. Additionally, in April, we announced the acquisition of Icon Capital Corporation, which has approximately $800 million in assets in the Houston, Texas market. Since we had the opportunity to discuss this transaction on our first quarter call, I won't go into great detail on this transaction other than to say, Icon continues to perform at a very high level and they're growing. They achieved loan growth of just over 7% annualized for the second quarter, which is a notable accomplishment, given the additional competitive pressures associated with the transaction announcement last quarter. We are anxious to have their bankers officially become a part of our team and in fact, their shareholders approved the merger yesterday at a special shareholder meeting.

I will now turn to John and allow him to discuss our financial results in more detail. John?

John Gary Copeland - *BancorpSouth Bank - Senior EVP, Treasurer & CFO*

Thanks Dan, and good morning, all. If you'll turn to Slide 4 in the slide deck, you'll see our summary income statement. I'd like to remind everyone again of the impact that the 2 merger closings in January had on the comparisons shown here. The transactions closed effective January 15, which resulted in 2.5 months of activity in our first quarter results. Accordingly, the second quarter is the first quarter in which we've reported a full 3 months activity from these mergers. In reviewing the summary income statement, net income was $54 million or $0.55 per diluted share for the second quarter. We had one meaningful non-operating item during the quarter, which was the $1.9 million in merger-related expenses.

Additionally, as Dan mentioned, we had a small negative MSR valuation adjustment for the second quarter of $200,000. Accordingly, we reported net operating income, excluding MSR, of $55.6 million for the quarter or $0.56 per diluted share compared to $53.6 million or $0.54 per diluted share for the first quarter of 2018 and $38.8 million or $0.42 per diluted share for the second quarter of 2017. Net interest revenue increased 2.9% compared to the first quarter of 2018 and 21% when compared to the second quarter of 2017. In addition to the incremental net interest revenue associated with the January acquisitions, we also saw continued expansion in our net interest margin, as a result of core spread increases. Our reported net interest margin for the second quarter was 3.71%, while our net interest margin, excluding accretable yield, was 3.63%. Comparable metrics for the first quarter of 2018 were 3.67% and 3.60%, respectively.

We reported a net interest margin of 3.52% for the second quarter of 2017, which was not impacted by purchase accounting accretion. And looking at our core margin, the pickup in loan yields continues to outpace the increase in deposit costs. Our loan yield, excluding accretion, increased by 6 basis points compared to the first quarter of 2018, while the total deposit cost increased by 3 basis points. We also continued to receive benefit from the repricing of our securities portfolio.

Our taxable available-for-sale securities yields, which comprised the largest component of our portfolio, increased 5 basis points quarter-over-quarter.

Before we move on, I'd like to mention one other item, our effective tax rate for the quarter was 19.2%, compared to 21.7% for the first quarter. This decline was driven by a back tax benefit of approximately $2 million associated with the appreciation of stock awards that divested during the quarter.

If you'll turn to Slide 5, you'll see a detail of our noninterest revenue streams. Total noninterest revenue was $72.5 million for the quarter, compared to $68.1 million for the second quarter of '17 and $78.9 million for the first quarter of 2018. Outside of the swings in the MSR asset valuation, virtually, all of our noninterest revenue streams were stable for the quarter. The increase in insurance commission revenue compared to the second quarter of last year was driven primarily by the accounting revenue recognition change related to contingent commissions, which we discussed at length in our first quarter call.

Additionally, our first quarter 2018 results included a $3.0 million legal settlement and a $2 million gain on the liquidation of subsidiary that were included in the other noninterest revenue. These were the primary drivers of the second quarter decline shown in this line. Otherwise, there were no significant unusual or unexpected items in our second quarter noninterest revenue results.

Slide 6 presents a detail of noninterest expense. Total noninterest expense for the second quarter was $145.2 million compared with $147.7 million for the first quarter of 2018 and $127.6 million for the second quarter of 2017.

There was some lumpiness in some of the line items, and I would, again, remind you that the January mergers have closed -- January mergers did have some effect on that. The only nonoperating item included in the quarter was the $1.9 million in merger-related expenses, which is down from $5.7 million in the first quarter of 2017. The only other change of significance was the decline in other miscellaneous expense. If you recall, we did have one large forgery and theft loss totaling $2.3 million in our first quarter results and this quarter, we had a related $1.3 million recovery.

Our operating efficiency ratio, excluding MSR, was 66.4% for the quarter, compared to 66.8% for the first quarter of 2018 and 67.3% for the second quarter of '17. We're pleased that this metric continues to decline. We are also optimistic about the opportunity to continue the improvement during the second half of the year, as we realize more of the cost savings associated with the 2 mergers. That concludes our review of the financials. Chris will now provide some color on our business development.

Chris A. Bagley - *BancorpSouth Bank - President & COO*

Thank you, John. Slide 7 reflects our funding mix as of June 30, compared to both the first quarter of 2018 and the second quarter of 2017. Again, as a reminder, the mergers with Central Community Corporation and Ouachita Bancshares closed January 15. Thus loan and deposit comparisons to quarters in the prior year should be viewed accordingly. Deposits and customer repos had declined $479 million, compared to the first quarter of 2018.

As Dan suggested, the first quarter is typically high due to seasonality in public funds and the second quarter decline we experienced is largely attributable to this anticipated seasonal decline in public fund money as well as customer federal tax payments. While the decline in deposits is not totally unexpected, we continue to focus on relationship banking and development of core deposits. This is also reflected in the overall mix and the increase in noninterest demand balances.

We will continue to compete in our markets with a disciplined approach to pricing. As we look at geographical performance relating to deposits, we have 4 community bank divisions standout this quarter for deposit growth: Dallas, Texas, Houston, Texas, Central Arkansas and Gulf Coast divisions all reported excellent results this quarter.

Moving to Slide 8. You'll see our loan portfolio as of June 30, compared to the first quarter of 2018 and the second quarter of 2017. We reported net loan growth of $121 million or 4% on an annualized basis for the second quarter. As Dan mentioned, there is always elevated competitive pressure and potential runoff in markets experiencing mergers and conversions. Having gone through 2 conversions in the first half of 2018, we are particularly pleased with this level of loan growth for the quarter and the ability of our new merger partners had exhibited in holding on to relationships during this transition. As we look at our second quarter of lending efforts from a geographical perspective, we had several divisions produced meaningful loan growth. Standout divisions for the quarter are Dallas, Texas, Houston, Texas, Tennessee Metro, and our Pineville divisions.

Side 9 contains credit quality highlights. I'd like to touch briefly on a couple of these bullets. We had a provision for credit losses of $2.5 million for the second quarter, compared with a provision of $1 million for both the first quarter of 2018 and the second quarter of 2017.

The provision for the quarter was sufficient to provide for the loan growth achieved during the quarter as well as cover the net charge-offs of $2 million. Allowance of the percentage of net loans and leases were stable at 0.97% and 1.05% net of acquired loans accounted for under the purchase accounting rules when compared to the first quarter. In addition to the continued low level of net charge-offs, other credit quality indicators are trending in a positive direction as well.

In reviewing year-over-year trends, total NPLs to net loans and leases have declined to 0.59% from 0.65% a year ago, while NPAs to net loans and leases have declined from 0.72% to 0.65% over the same time period. Credit quality will continue to be a primary focus of our team, as we move forward.

Moving on to mortgage and insurance. The tables on Slide 10 provide a 5-quarter look at our results for each product offering. Our mortgage banking operation produced origination volumes for the quarter totaling $523.7 million.

Home purchase money volume was $420 million or 80% of our total volume for the quarter. Deliveries in the quarter were $303 million, compared to $215 million in the first quarter of 2018 and $264 million in the second quarter of 2017.

Production and servicing revenue, which excludes the MSR adjustment, totaled $7.1 million for the quarter, compared to $7.7 million for the first quarter of 2018 and $7.6 million for the second quarter of 2017. Our margin was 1.75% for the quarter, representing a decrease from 2.44% for the first quarter of 2018.

This margin decline is common during the second quarter each year, as our pipeline stabilizes during the middle of the annual selling season. As we've said in past calls, we view a stable pipeline margin to be in the 1.75% range, and you can certainly see that in Q2, as the pipeline was flat quarter-over-quarter at $260 million at June 30 and March 31. Finally, as Dan mentioned earlier, the MSR valuation adjustment during the quarter was a negative $0.2 million, which is insignificant to our quarterly results.

Moving on to insurance, total commission revenue for the quarter was $33 million, compared to $29.1 million for the first quarter of 2018 and $31.1 million for the second quarter of 2017.

As we've mentioned in the past comparable quarter, prior year comparisons are more relevant due to seasonality in the book of business. However, that comparison for this year will be impacted as a result of the accounting revenue change that John mentioned earlier.

Contingent commissions are now estimated and recognized throughout the year, rather than in the period of cash received. These commissions are included within the other component of insurance commission revenue, which is up $1 million, compared to second quarter of 2017. All that to say, the property and casualty and life and health commissions are up 2.8% in aggregate over the same period last year.

This growth rate is consistent with the message we've been communicating for some time now. We continue to experience a soft market in terms of insurance pricing. Our team is seeing very little opportunity for revenue growth on pricing alone. Nevertheless, they are out there daily calling on customers in effort to grow our booking business and expand relationships and revenue. If we can continue to build our customer base, we will be well positioned when insurance pricing does cycle and firm. Now I'll turn it back over to Dan, for his concluding remarks.

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Thanks, Chris. I'm extremely proud of our team's effort to improve our performance. All of our frontline teammates, including our bankers, mortgage team, wealth management team and insurance team, contributed to our growth efforts during the quarter, despite various challenges unique to each of their product offerings. Additionally, team mates in our back-office and support areas continue to improve their respective processes and support our growth effort without increasing our overhead.

These efforts continued to yield improved financial results. We reported record earnings for the second consecutive quarter, while our operating return on assets, excluding MSR, topped 1.3% for the first time in our company's history. As we look forward, I'm confident we have the opportunity to continue this trend. We believe our net interest margin will continue to benefit from recent rate hikes, as our loans and securities reprice. Additionally, we expect to continue to harvest cost savings from our recent merger integrations. I'm excited about the benefit of these opportunities, along with a continued focus on taking care of our customers will provide to our performance in future quarters. With that, operator, we'll now be happy to answer any questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question comes from Jennifer Demba with SunTrust.

Jennifer Haskew Demba - *SunTrust Robinson Humphrey, Inc., Research Division - MD*

Two questions. The cost savings estimates you have for the 2 deals that closed -- or for the ones that are closing this year, do you think that you have a chance to beat those? And if so, in what area would that come from? And then second, if you could just clarify your interest and capacity to do more acquisitions and if you're interested, kind of frame what you are looking for right now?

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Sure. Okay, cost savings on the 2 transactions that closed in January. They're both a little different as you know, so we had market overlap in North Louisiana, that integration took place in February. Those 2 teams are actively engaged. I think we're well past the significant noise that comes with operational integration in North Louisiana. Kevin Koh is our Division President in that market, was the CEO of OIB and he's done a fantastic job of leading his team. The cost savings there come through branch consolidation. So you've got the standard back-office synergies that come and in addition to that, we had multiple branch overlap and branch consolidation that will benefit us long term. We continued to harvest some of that cost saving over there, some of it is already in place. In fact, I'd say a big slug of it is in place, was not in place for the full quarter, but was in place during the quarter. And so as we finish the second quarter, we'll get the full benefit of the lion's share of savings out of OIB in the third quarter. The second operational integration of 2018 for us was in Central Texas, with the First State Bank of Central Texas and Don Grobowsky's team over in Austin, Temple-Killeen area. That integration took place in June. And so we are just beginning the process of harvesting off some of the back-office synergies that will come from that. So we will not see a full quarter benefit from those savings in the third quarter, but we should have that in place by the end of the third quarter, so that we'll see a full benefit of that in the fourth quarter. Your specific question, I think, Jenny, was can we beat our internal targets? We think we can reach our internal targets and as we get to the end of the game, we want to make sure that we're winning. And so I suspect that our whole team is focused on trying to make sure that we're doing the right thing and becoming more efficient and doing that with integration of the 2 transactions that are there. The third transaction that's still out there was Icon. I've talked about them for a minute. I was in Houston yesterday for their special shareholder meeting to approve the transaction. We are in, what I refer to, as the hurry up and wait phase of the process, where the applications are in at the regulators. There has not been a lot of communication at this point. I would suspect in the next 30 or 60 days, we will start seeing or hearing or having questions coming back and forth on those applications.

And our intention to be -- to complete that here -- complete that merger here in the back half of 2018 and work towards an integration on that transaction. And then I think to that, you added on, what is our appetite or capacity for other transactions and what are we looking for. I don't think anything's changed from my comments or philosophy on that for some time. We continue to have active communications with lots of potential partners out there, from smaller transactions to the larger transactions. There is a lot of talk going on in M&A world today. A lot of people trying to pick the right partner. We're talking to lots of folks and that spreads across our entire footprint. We're looking for folks where there is a cultural fit, where there is a business model fit, where 1 plus 1 is going to be more than 2. And we continue to believe there are opportunities out there for us, we just need to make sure we find the right ones. How'd that do, Jenny?

Jennifer Haskew Demba - *SunTrust Robinson Humphrey, Inc., Research Division - MD*

That's great. One follow-up, if I could. So are we looking at a couple of million dollars of cost savings over -- coming in over the next couple of quarters? Is that a good way to think about it?

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

I don't have a number in my head, John's going to have to jump in here with me. But when you look at their overall run rate, the 2 banks combined had an overall run rate of $50-plus million a year in operating cost coming into '17, and I think we said we were in the 20-plus percent cost savings over both of those going forward. So I think you can figure that out.

Operator

The next question comes from Jon Arfstrom with RBC.

Jon Glenn Arfstrom - *RBC Capital Markets, LLC, Research Division - Analyst*

Question for you Dan, or maybe Chris. Can you talk about the magnitude of some of the runoff from the acquired banks, just kind of curious if you could maybe get us to a core growth number and what kind of expectations you have going forward?

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

I don't have a specific number, Chris can jump in here. We continue to experience ebbs and flows, and in any transaction, you wonder kind of what your competitors are going to do. I think, again, the OIB transaction -- integration was earlier in the year, it was in February. And I think the noise from that is gone. So that team is more focused today on doing what they do, which is go out and bring in new customers. And hopefully, they're shifting from defense to offense, which means, we're hoping we can grow in that market. Over in Central Texas, we've been playing defense longer. So I think that's where the risk is, is that we're saying that when you're not playing offense and you're playing defense, the risk of losing is there. Our team across our entire footprint continues to look for and challenge, but from a pricing and structure competition, their competition is out there. Chris or John may want to jump in here, but we're continue to see price competition that makes us scratch our head. In some cases, term or structure competition that -- we -- this is not when we want to stretch. Chris?

Chris A. Bagley - *BancorpSouth Bank - President & COO*

That's right. I think, to start with, I think the cultural fit with OIB and FSB was very positive and that translates or flows through to their customers. So we have a good -- we have a good -- they're good relationship bankers just like us, so we feel good about their customers. I think that's helping to protect some of that. They're doing a great job at protecting business. But like Dan said, it's very competitive, it's a rising rate environment. Maybe a little more risk on the deposit side, because that move -- tends to move quicker and loans with -- that were priced a year ago may have a tendency to want to stay. But any time this happens, all the local banks take advantage of in trying to move customer relationships over. And so that's what our folks are doing in the FSB and former OIB world today is protecting that existing customer base, try to keep it where it is. And as Dan says, they can turn to offense and -- once they get all of their new processes and procedures under their fingertips.

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Yes, John's pointing out in our presentation -- in press release, there's some information about the outstanding balance on the acquired loans and the principal pay downs in that book, Jon, was about $180 million.

Jon Glenn Arfstrom - *RBC Capital Markets, LLC, Research Division - Analyst*

Yes, a pretty common complaint, I guess, from others in terms of the competitive environment. But -- pretty common. So I guess, the message here is, you're still maybe thinking mid-single digit growth, maybe a little bit better if you can curtail some of the runoff. Is that a fair way to think about it?

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

That's right. I think, at the end of the day, 4% is -- we're pleased. And I think when you look at the total -- if the total company, including all the noise behind the $1 billion-plus that we brought in, $1.5 billion that came in, I think we're pleased with where we are. But we're pushing the team, we need to continue to get better.

Jon Glenn Arfstrom - *RBC Capital Markets, LLC, Research Division - Analyst*

And then Chris, just one small one. The mortgage margin, any thoughts on what that could look like going forward? You guys -- I mean, given the decline in the margin, I understand your comments about basically, where you expected, I thought you had a pretty good quarter, but given the pipeline, where it's at, any thoughts on what we might see for Q3?

Chris A. Bagley - *BancorpSouth Bank - President & COO*

Our margins -- I can't -- we can't predict that, because it depends on the pipeline and it moves up and down based on what that looks like. But we've always said our margins should be around the 1.75% and it's stable. I think, that was evidenced this quarter. We're not competing on margin, we're trying to hold our margin where it is. We're seeing some pockets of competition where they're being more aggressive on their margin and we're not having to do that yet across the footprint.

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Jon, when we look back, I think, 2 or 3 or 4 quarters ago, we were talking about how to determine what our normal stable margin was, and we said then that we think that we've got a 1.60% to 1.75% core margin with a flat pipeline. We've never had a flat pipeline before. This quarter, it's pretty darn flat and we have reported a 1.75% margin. So I think we feel like we're right where we thought we would have been with a flat pipeline.

Operator

The next question from John Rodis, FIG Partners.

John Lawrence Rodis - *FIG Partners, LLC, Research Division - Senior VP & Research Analyst*

A question on fee income. The card-based line item, you showed about a linked-quarter increase of about $1 million. Was there anything unusual? I know, you guys said there wasn't really anything out of the ordinary, but what sort of drove that increase in the quarter?

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

I think most of that is probably merger activity. Remember, you've got some trailing stuff coming through. One of the things we didn't -- I don't think any of us talked about too directly in our comments, remember, we did not have a full quarter in 1Q of the 2 merger partners. They came in on January the 15th and so you've got some lagging stuff coming through behind that. This quarter, we had a full quarter on both of those transactions, which would be a full quarter on card revenue, a full quarter on transactions and also a full quarter on expenses that I think maybe some folks did not fully bake into their numbers out there on your side of the isle when they were looking forward from an expense run. So we -- this was a true quarter where the 2 mergers were there the whole time. I think that's the difference on card revenue.

John Lawrence Rodis - *FIG Partners, LLC, Research Division - Senior VP & Research Analyst*

So if card revenue's going to be higher, then expenses should also be higher for that line item, correct?

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Yes, I think you had a full run rate of expenses in the quarter. So again, if your question is, is some of the expense in 2Q related to higher expense on the card revenue that was generated, I guess that logically makes sense to me. I don't know whether I have seen it that way. John, you want to...

John Gary Copeland - *BancorpSouth Bank - Senior EVP, Treasurer & CFO*

No, we haven't analyzed this in that fashion, but it makes sense.

John Lawrence Rodis - *FIG Partners, LLC, Research Division - Senior VP & Research Analyst*

Okay. And then Dan , just a question on the balance sheet. You saw a little bit of runoff in the securities portfolio. Do you expect it to sort of stabilize? How should we think about the level of securities going forward?

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

John, you want to jump in on that?

John Gary Copeland - *BancorpSouth Bank - Senior EVP, Treasurer & CFO*

Yes, it should be fairly stable. The good news is we've got some really good repricing opportunities in the securities portfolio. We've got probably $1 billion repricing in the next 18 months from a $120 million to $250-plus million, so that's a great opportunity for us there.

John Lawrence Rodis - *FIG Partners, LLC, Research Division - Senior VP & Research Analyst*

And then if I may, just one last question on the tax rate. I think you said a $2 million benefit from stock-based compensation, so if you add that back, it looks like your effective rate was 22% to 22.5%?

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

They're looking at each other.

John Gary Copeland - *BancorpSouth Bank - Senior EVP, Treasurer & CFO*

Yes, adding that back, yes. Yes, that's correct.

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Yes, the rate was 19.5%.

John Gary Copeland - *BancorpSouth Bank - Senior EVP, Treasurer & CFO*

The rate was 19%. I was...

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Yes, John's got 19% in his head. If you add back the benefit from the stock-based compensation.

John Gary Copeland - *BancorpSouth Bank - Senior EVP, Treasurer & CFO*

That's correct.

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

It is a unique second quarter '18 event, then you're -- we're closer to -- we're over 22%, close to pushing 23%.

John Lawrence Rodis - *FIG Partners, LLC, Research Division - Senior VP & Research Analyst*

And I think last quarter, you sort of said 23% is a good rate, is that sort of still....

John Gary Copeland - *BancorpSouth Bank - Senior EVP, Treasurer & CFO*

It's still pretty good, yes.

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Yes.

Operator

The next question comes from Matthew Olney, Stephens.

Matthew Covington Olney - *Stephens Inc., Research Division - MD*

Dan, within the mortgage discussion, it looks like you portfolio-ed a more significant portion of the production in the second quarter. Any reason why this strategic shift or more just the unusual timing issue?

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Yes, I don't think there's any strategic shift there at all, that's just product mix. So when we look at our products that we're selling, there are some seasonality in some of those products and some of the products that get pushed through our portfolio of products that the mortgage lenders are pushing and the portfolio of product was popular in the second quarter. I think when you look back, you would have seen that we had a pickup in portfolio of product in second quarter of last year also. So I don't think there's any really shift in process. Chris, you've got your answer there.

Chris A. Bagley - *BancorpSouth Bank - President & COO*

No, Dan answered it well. There's just certain products that we -- that our portfolio of products that we move through the mortgage team and it shows up in those numbers and there's some seasonality to it.

Matthew Covington Olney - *Stephens Inc., Research Division - MD*

Okay. And then on the deposit side, you gave us a good commentary on competition on the loan side, but on deposits, anything that you can call out as far as any pressures you're seeing in any of your markets more so than other markets?

John Gary Copeland - *BancorpSouth Bank - Senior EVP, Treasurer & CFO*

No, they're all over.

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

It's everywhere.

John Gary Copeland - *BancorpSouth Bank - Senior EVP, Treasurer & CFO*

Most of it's coming from deposit specials. Everybody is running a special, so that's where we're seeing it. But it's across the footprint, across all competition.

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Yes, deposits are obviously very important. We've got a very stable, very core, very loyal core customer base and we like that. I think many folks like you have said that's a core strength of our company, but you can clearly see that the folks that are out there, that are chasing deposits, are continuing to ratchet up the pressure and that's happening across our footprint.

Matthew Covington Olney - *Stephens Inc., Research Division - MD*

And on that note, Dan, a lot of your competitors this quarter did move some of their posted rates over the last few months and based off your results in 2Q, it looks like you didn't require that. Can you just talk about kind of what's your response to that competitive pressure?

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James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

We did raise posted rates on almost every product throughout the quarter. And some, again, late in the quarter. So remember the last rate hike was, what, June -- basically, June the 15th, I don't remember exactly what date, but mid-June was the last rate hike and post that rate hike, we raised posted rates on almost every product. So we continue to look at our products and our pricing. We've got a process in place that's seeing that almost on a -- not a -- necessarily a daily basis, but certainly, a weekly basis. We're seeing what's happening, and we're listening to what our folks are telling us. So being nimble, being able to move quickly, is important to us, and we give our folks in the field a lot of autonomy to compete on that.

Matthew Covington Olney - *Stephens Inc., Research Division - MD*

So just to clarify, it sounds like you did move the rates kind of late in the quarter and we'll get the full quarter impact of that in 3Q. But giving your earlier commentary about the core margin expansion in the near term, it sounds like you still expect that, even with a little bit higher deposit betas in 3Q versus 2Q. Is that a fair way to look at it?

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Yes, we continue to model where we believe that we've got upward pressure on margin, because we continue to harvest the repricing on the -- when you look -- frankly and our own pricing was up 6 bps, is that right? So lots of folks had much higher up on the loan yield. We're going to continue to see that loan yield run up over time as those repricing dates hit on the loan book. So we continue to believe we've got upward margin pressure.

Matthew Covington Olney - *Stephens Inc., Research Division - MD*

Okay, helpful. And then just shifting over towards the allowance discussion and curious what your expectations are for provision expense for loan losses? It looks like in 2Q, $2.5 million provision expense, a low relative number, but I guess still a high that's been for a while. So what is your outlook on the provision expense from here?

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Yes, a couple of things in there. So in the second quarter, we divested some ORE that I would have said was stale ORE. We actually ran an auction for some ORE that was quite old. And some of the charge-off is that. So hopefully, we're not seeing that off of the current stuff that's out there. But I do think any time you've got an acquired book and as those loans are transitioning from the acquired book into the book that is in your loan loss reserve, that's going to force your loan loss reserve modeling to recognize those new credits that are coming into the formula. Chris?

Chris A. Bagley - *BancorpSouth Bank - President & COO*

It's a -- Matt, it's a modeling discussion. The model drives it, but some of the things that can drive that model are loan growth and charge-offs. And probably, what we're going to experience in the next few quarters are transitions from purchase to acquired loans to what -- they turn into legacy loans, for lack of a better term. So when they get touched or renewed, that formerly purchased loan becomes a loan that's in your ALLL model. So it -- there's going to be a lot of moving parts within that that's hard to predict. But it is all just model drift, that's what will drive it.

Operator

The next question comes from Michael Rose from Raymond James.

Michael Edward Rose - *Raymond James & Associates, Inc., Research Division - MD, Equity Research*

Just one from me on just credit, in general. We've seen a couple of one-offs at some other banks this quarter. Just more broadly, any early warning signs that you're looking for? Is there any certain industry verticals that you're maybe a little bit more cautious on? Clearly, pricing and structure has remained competitive, gotten more competitive in some cases. So just any general comments there would be helpful.

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

No problem, Michael, good to hear from you. I hope you're staying cool in your markets. The -- as we said earlier, pricing and structure continue to be headwinds in our loan acquisition or loan acquire process, as we're looking to go out and acquire and find and harvest new loans out of the market, competition is very tough on both fronts. When you talk about credit quality, we continue to not see any -- we haven't seen a one-off here, we haven't seen any signs in any of our books that causes great concern for us. We're watching all the things that are there. You see our 30 to 89 day number ticked up in the quarter. I think -- again, I think that's probably more seasonal. It's also, again, first full quarter for acquired loans to be in the book. And so we're trying to understand what's normal in those acquired books compared to ours. But I don't think we're seeing anything. Chris, you talk to our lending guys, our Chief Lending Officer, what are you hearing?

Chris A. Bagley - *BancorpSouth Bank - President & COO*

It's positive. All the credit metrics are moving in the right direction from -- we look at a lot of different things on an ongoing basis. If you -- if you ask us what we were looking at or thinking about, and one of the things we're thinking about on the commercial side is as loans reprice with -- at higher rates than were underwritten 2 and 3 years ago, could there be some stress on some of those cash flow coverages, and we feel good about how our underwriting was done at the time, but I think we're going to see some of that as an industry over the next 25 months or so.

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Yes, I remember, our average loan size continues to be very small, so the very granular nature of our portfolio, we've just got lots of credits. We're not feeling stresses on the credit quality side at all at this point.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to Dan Rollins for any closing remarks.

James D. Rollins - *BancorpSouth Bank - Chairman, CEO & Director*

Thank you for joining us today. If you need any additional information or have further questions, please don't hesitate to contact us. Otherwise, we look forward to speaking to you again soon. Thank you all very much.

Operator

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