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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Great Southern Bancorp, Inc. Second Quarter 2018 Earnings Conference Call. (Operator Instructions) As a reminder, this conference may be recorded. I would now like to turn the conference over to Ms. Kelly Polonus, Investor Relations. Ma'am, you may begin.

Kelly A. Polonus - *Great Southern Bancorp, Inc. - Director of Communications & Marketing for Great Southern Bank*

Good afternoon, and welcome. This is Kelly Polonus, Investor Relations for Great Southern Bancorp. The purpose of this call today is to discuss the company's results for the quarter ending June 30, 2018.

Before we begin, I need to remind you that during the course of this call, we may make forward-looking statements about future events and future financial performance. You should not place undue reliance on any forward-looking statements, which speak only as of the date they are made. These statements are subject to a number of factors that could cause actual results to differ materially from the result anticipated or projected. For a list of some of these factors, please see the forward-looking statements disclosure in our second quarter 2018 earnings release. President and CEO, Joe Turner; and Chief Financial Officer, Rex Copeland are here with me. I'll now turn the call over to Joe.

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

All right. Thank you, Kelly, and good afternoon to everybody out there. Thank you for joining us for our second quarter earnings call. I'll provide some general remarks about the quarter and then turn it over to Rex Copeland, who will talk a little bit more in detail about the income statement. And then, of course, we'll open it up for questions at the end. We did have a very strong quarter, hopefully, all of you have had a chance to at least glance at our earnings release. If you have, you probably noticed that we are $0.97 a share, or $13.8 million during the quarter. Our performance metrics during the quarter were good, with 11.32% return on annualized common equity or annualized return on common equity. Our return on assets was 1.23%, and our margin was 3.94%.

Our second quarter earnings were really driven by two things, I think. First, an expanded core margin, which was certainly aided by outstanding loan growth during the quarter, and then good expense containment. We did have unusual expense -- an unusual expense item during the quarter. At the end of the second quarter, we made the decision to reduce prices on some sticky ORE -- sticky parts of our ORE portfolios. That resulted in a $2.1 million or $0.11 per share decline in our expenses that reduced our earnings. We have though, and it's very preliminary, obviously, because we're only three weeks into the third quarter, but we have seen really good activity on our ORE portfolio, particularly, on the parcels where we reduced prices. So we think we did the right thing there. We continue to feel really good about our loan portfolio, both the production and the quality of the portfolio. As you saw in our earnings release, our outstanding loan balances have increased about $133 million from the beginning of the year and about $100 million from the end of the second quarter.

The increase was primarily in commercial real estate, multi-family and one- to four-family residential mortgage loans. Our pipeline also continues to grow, it's up about $120 million from the end of 2017. So again, we feel really good about that.

Overall, I think our asset quality continues to improve but we're coming from really low levels of problem assets, so the improvement is relatively minor and relatively slow.

But our level of nonperforming assets did decrease by $5.9 million. During the quarter, nonperforming loans decreased by $1.2 million and ORE increased -- decreased by $4.7 million.

So good improvement in the levels of our nonperforming loans.

Our levels of potential problem loans increased $945,000 from the end of March. That was mainly driven by the addition of a $2 million relationship, which was briefly described in our earnings release.

Our capital position continues to improve. Capital at the end of June was $490 million, that's $18.6 million higher than it was at the end of the year. About 10.7% of total assets. Book value per share has increased to $34.69 from $33.48 at the end of the year.

As far as business initiative, tomorrow we do expect to close our Omaha transaction, and that's going to result in a $7 million gain. I think it's going to allow us to sort of marshal our managerial resources in the markets where we're having more luck. We are keeping though an Omaha loan production office, which is extremely important to us, and we're excited about keeping those folks on board.

As we told you when we announced the sale, at that time, we expected it to be slightly positive from an earnings perspective, but that was -- we told you as earnings -- as interest rates increase, that it will get probably closer and closer to the breakeven proposition on an ongoing basis. And I would say, Rex, it's probably closer to breakeven, as an ongoing. But we're still pleased with the parameters of that transaction. We also have opened or will open in the first week of August, loan production offices in Atlanta, Georgia and Denver, Colorado. Those will both be staffed by veteran lenders, probably 30-year kind of lenders in each of those markets. And we expect good things out of those folks. So that concludes my prepared remarks. At this time, I'll turn over the call to Rex Copeland.

Rex A. Copeland - *Great Southern Bancorp, Inc. - Treasurer*

All right. Thank you, Joe. I'll talk first about net interest margin. As mentioned earlier, the reported margin was 3.94% in the second quarter. Our core net interest margin, which is going to exclude the impact of additional yield accretion that we recognize on the FDIC acquired loans increased to 3.84%. That was an increase of 28 basis points and three basis points from the year-ago quarter and the most recent quarter respectively.

The primary driver of the margin expansion continues to be increased yields in most of our loan categories, and that's partially been offset by a gradual but steady increase in deposit cost. And you could see that in some of the information that is provided in the earnings release.

Also, one thing that helped drive our earnings this year was the lower income tax expense and lower income tax rates that we experienced now versus a year ago based on the legislation that was passed in December.

So we've told you before and indicated in previous filings that rising interest rates may have a modest positive effect on our net interest income and margin. And so far that's been borne out as we've seen the rate increases from the Federal Reserve. We expect those similar effects moving forward. Competition does remain very significant for us. And as I've said, increased deposit cost and other borrowing costs are anticipated and will likely put a bit of pressure on that margin expansion.

We've also had headwinds to our margin expansion, somewhat by reduction in our consumer loan portfolio, and we've talked about that for quite a while now. And we're continuing to see net runoff on the consumer loan portfolio each month, really. We are originating loans, but the repayments continue to exceed the originations.

And so our cost generally speaking on deposits we think will increase, but we did see more of an increase in the second quarter this year than we experienced in the first quarter as far as deposit rate percentages. Also cost on our other borrowings are good, which will generally be affected by changes in LIBOR rates, as we do a lot of short-term borrowing from the Home Loan Bank.

Noninterest income during the quarter ended June 30, our noninterest income decreased $8.3 million compared to the year-ago quarter. You may recall in the year-ago quarter, we had some fairly significant items, the largest of which was the termination of the Inter Savings Bank, FDIC loss sharing agreement.

We recognized the gross gains of about $7.7 million in noninterest income on that last year second quarter. Other income, last year, we had some higher income related to some interest rates swaps that we entered into, which -- that was not repeated in the second quarter this year and then also some late charges on our prepayment penalties on some larger payoffs last year, second quarter versus this year.

So some of those things were sort of unusual, obviously, the biggest item being the gain on the termination of the loss sharing agreement last year. Joe mentioned earlier, expense containment, and I think our expense containment and operational efficiency remain a focus of our company, I think we did a good job of that in the second quarter.

Obviously, the reported number was higher this second quarter versus the year-ago second quarter and also the first quarter of this year that driver of that was related to the $2.1 million write-down on some of our foreclosed assets that we took this year second quarter that Joe mentioned. When you remove that, I think our expenses were very much in line with the last few quarters, and what we kind of have been seeing as a run rate. We also identified a few other smaller items in our earnings release that related to noninterest expense. But again, we feel like our core operating expense level has remained stable. That concludes, I think, the remarks that we had at this time. And so we will entertain questions now.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And the first question will come from the line of Andrew Liesch with Sandler O'Neill.

Andrew Brian Liesch - *Sandler O'Neill + Partners, L.P., Research Division - MD*

All right. Just a follow-up here on the margin. So it sounds like funding costs are going to continue to march a bit higher. So this [394] level on a reported basis. Is that kind of like a plateau and will drift lower from here. Then again, just similarly on a core basis with the [384]. Is that kind of a top or maybe hold steady?

Rex A. Copeland - *Great Southern Bancorp, Inc. - Treasurer*

It's hard to say, exactly. It is kind of what the Fed does. Our anticipation is, I think, along with -- so what the consensus is that the Fed's not going to raise rates in August, but probably will raise 25 basis points in September.

So we will get the benefit of that, until late in the quarter. But a lot of our loans are tied to LIBOR and so as LIBOR anticipates that, we do have loans that generally reach that on the monthly basis and some every three months. So we do start to see some benefits on that.

I would just say that we are seeing competition in our markets on deposits and trying to walk the balancing act of raising rates selectivelywhen we need to and try to utilize our various funding sources in the most advantageous way we can. But certainly, we're going to see, I think, the cost of deposits and the cost of borrowings going up a little bit more. I'd say the percentage rise or the Beta on those cost has not been as high maybe as what we had sort of anticipated it could be.

So we're continuing to try to manage that increase as best we can. So it's hard for me to answer that question specifically or concretely...

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

But I think the only thing I would add to what Rex has said is that it does seem like the benefit, the increase in net interest income on loans when rates do increase comes a little more quickly than the deposit cost. So yes, I think generally, it's fair to say once the -- you can't even say that Fed stops raising rates once, LIBOR stops increasing, then I think we will have some catch up probably on deposit rates for a little while thereafter.

Andrew Brian Liesch - *Sandler O'Neill + Partners, L.P., Research Division - MD*

Got you. And then just on the expense side, done a good job just keeping expenses here to kind of stable not including the foreclosed assets cost around $27.2 million. Recognizing that you've hired some folks in these new markets. I would imagine that the expense is built from here. So I'm just kind of curious that where you think a good run rate might be for operating costs?

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

Well, again, we don't really give forward guidance. I think as you think through your models, those are things that I would encourage you to keep in mind would be the opening of those LPOs. But those aren't extremely expensive. You have maybe put staff with a total of four people to start and then some rented office space. So those aren't extremely expensive propositions. And then beyond that, we're going to have annual increases for our people. But generally, I think, we feel like there's operating leverage. We feel like we should be able to grow our company without commensurate growth in our operating expenses.

Rex A. Copeland - *Great Southern Bancorp, Inc. - Treasurer*

And just in the operating expense section, we will be reducing some costs there with the four branches...

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

Yes, that we will do, that we close here tomorrow.

Rex A. Copeland - *Great Southern Bancorp, Inc. - Treasurer*

Yes, I think we said that it's going to be about $1 million a year or something.

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

$1 million, $2 million.

Rex A. Copeland - *Great Southern Bancorp, Inc. - Treasurer*

$1 million to $2 million.

So that will reduce our operating expenses, and the sale as we said will reduce our, probably, noninterest income by a little bit, because it does generate a little bit of noninterest income and then just the funding cost of the net difference in the deposits versus what they're paying us for the premium and the fixed assets.

Operator

And the next question will come from the line of Michael Perito with KBW.

Michael Anthony Perito - *Keefe, Bruyette, & Woods, Inc., Research Division - Analyst*

I wanted to start maybe on the two new offices and Joe, maybe, kind of high-level question for you. Obviously, there's -- whether it's the team specifically or the markets themselves. I'm sure there's something that is drawing you to both Atlanta and Denver that some form of opportunity there. But I guess, how do you guys measure the cost and kind of the franchise impact, I guess, of moving to new markets versus maybe spending resources on expanding the team you have in the current markets that you're already in?

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

Well, I don't think the two are mutually exclusive. It's really about opportunity. I do think you have, at least, we found it that you probably have maybe more opportunity to grow your loan portfolio by going into a new market like that. Because you're not -- as opposed to hiring a new person in an existing market. Most of our existing markets, we think, are well-staffed, it's not that we wouldn't add people, if we could find them. And I guess that's my bigger point. It's more about finding the right people. And both of the people we've hired in Denver and Atlanta are very strong lenders there, very seasoned lenders. And we think both Denver and Atlanta are vibrant market places that will allow us opportunity for growth. And of course, we have loan production offices in Dallas, Tulsa ...

Rex A. Copeland - *Great Southern Bancorp, Inc. - Treasurer*

Chicago.

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

Chicago and soon Omaha. And Dallas and Tulsa are the most mature of those and they are very profitable endeavors for us. And we expect good things out of Atlanta and Denver as well.

Michael Anthony Perito - *Keefe, Bruyette, & Woods, Inc., Research Division - Analyst*

Helpful. And maybe on Chicago, specifically, obviously, to market that seen some disruption recently. Is there any thoughts on may be trying to be more aggressive there? Or have you seen any greater opportunity to maybe scale that, that's particular LPO to hope, maybe reach the level you're at in Tulsa or Texas as examples you just mentioned?

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

You mean by hiring more people or by just being more aggressive on the lending front?

Michael Anthony Perito - *Keefe, Bruyette, & Woods, Inc., Research Division - Analyst*

Yes. I mean it's just, obviously, there was a major mid-market competitor that was acquired by a large regional that's historically struggled in the market. So I was just curious -- I guess, more -- maybe a more basic question. Have you started to see any fallout from that or do you expect to -- and could that accelerate your build-out in that market?

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

We would certainly be open to that. I don't think we've really seen that yet, Mike. But we would certainly like to take advantage of that. We have taken advantage of similar situations, certainly in Springfield, in our Missouri markets when competitors have really, really well-regarded competitors have combined in a larger institutions, out of town institutions, that's generally has been a favorable thing and hopefully that will be true in Chicago as well.

Michael Anthony Perito - *Keefe, Bruyette, & Woods, Inc., Research Division - Analyst*

Okay. And do you envision these kind of this -- the broadening of the geography. I mean, one thing I think that we're -- I'm hearing a lot this quarter is just the competition on the asset side. Rex, you mentioned on the deposit side. But just in terms of how competitive it is getting both term structure pricing on the loan side. I mean, is there hope that by entering these newer markets it kind of broadens the pool of credits that you bring in to your credit team with the hope to maybe be able to close on more without having to sacrifice too much on the term or pricing side.

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

Right. That's absolutely it. We've always said, the more deals we look at, the better chance we're going to have to grow our company while maintaining our credit and pricing discipline. So that's 100% it.

Michael Anthony Perito - *Keefe, Bruyette, & Woods, Inc., Research Division - Analyst*

Okay. And then so just looking at the stock chart, obviously, year-to-date, your shares have done fairly well. And there was no share repurchase in the quarter. And I guess two-part question here. I'm curious if, one, at the current level, the share repurchase isn't all -- isn't a very attractive capital deployment option to you guys at this point. And your thoughts there? And then secondly, is there any thought. It seems like growth is actually kind of picking up here, especially with the auto rundown presumably slowing, which is good, but I mean, there's still plenty of capital. I mean, is -- any thoughts around the dividend policy, the payout accelerating that, or just any thoughts on those two items would be helpful.

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

Yes. I mean, I think, obviously, as our price goes up, share repurchases become relatively less attractive. I can't remember, I did the numbers sometime back, Mike, and I think at a $53 level, there was like a five-year earn back or something. And obviously, you would analyze a share repurchase differently than you would a -- buying another company. But at $59 or $50 a share, whatever we're trading at right now, those numbers get maybe slightly less favorable. Our earnings were very strong, and core earnings, earnings that we feel good about and so we will need to continue to examine our dividend in light of strong earnings and a very strong capital position.

Operator

(Operator Instructions) Our next question will come from the line of John Rodis with FIG Partners.

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

Let's see, I guess, a lot of my questions were asked and answered. But guys just back to the -- so the new SBA hire, the Atlanta and Denver offices, are any of those expenses -- were any of those expenses in the second quarter?

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

No, I don't think so. Very little. I don't even think the SBA was -- a person was in there. I don't -- he's on board already but I don't think he was in the second quarter.

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

Okay, so with the branch sales. If you save $200,000 to $250,000 a quarter. Do you think sort of those three initiatives maybe sort of offset those savings on a quarterly basis? Just sort of the modeling.

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

Probably, yes. I mean -- I think the new programs could be slightly higher. But I don't think it would be a lot.

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

Okay, okay. Guys, on page, I think, it's 16, the average balance sheet you guys always sort of put the end of the quarter date as far as where yields are and stuff. And this sort of back to the margin, it shows your spread would be down 10 basis points, I guess from the average for the second quarter. So that -- does that sort of, again, you guys talk about pricing pressure and stuff like that on the deposit side and loan side. Does that sort of point towards the lower margin or what are we missing?

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

I think that's going to do probably -- I saw that same thing, John, I think that's got more to do with -- the 3.72% includes the yield accretion, I believe, and the 3.62% does not. It would not, because our yield accretion was about $1 million during the quarter, which times annualize it that's $4 million, that would be about 10 basis points on our level of interest-bearing asset. Am I thinking about that right?

Rex A. Copeland - *Great Southern Bancorp, Inc. - Treasurer*

Yes, it is, John, if you went back and look at our previous earnings release and the first column there will be the marks, point in time, rate and yield. It was a little bit higher than two. But some of that has to do with the mix. This is a look at just the the actual days on June 30, what the assets and liabilities that we have and the rates on each of those and what that project out. And we did have a higher amount of cash on those days because we had about, well, $40 million or $50 million of loans that paid back in the last two weeks of June. You can probably see our average outstanding for the quarter was higher than -- or right around where our end of quarter balance ended up. So we did have some significant paydowns right at the end. So the mix on that particular day was round up for, say, $50 million lower in loans at the -- are at a higher rate and $50 million more in funds at the Fed that are earning us 2% or something like that. So some of that had to do with just the mix on that particular day as well. But as you can see that if you look back at this versus the March 31 point in time, the yields are higher but the expenses are higher as well. So I think that 3.62% -- I forget what the number was in the previous March, but it was a little bit higher than 3.62%, I think.

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

Okay. And back to this net interest income dollars, on a core basis, so it was a $40.4 million for the quarter. Was -- I mean, so there was nothing unusual in there as far as like elevated loan fees or anything like that?

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

No.

Rex A. Copeland - *Great Southern Bancorp, Inc. - Treasurer*

No.

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

No, I mean, we do -- from time to time, we will collect interest income on like nonaccrual loans like maybe we'll have a nonaccrual loan payoff that may feed into that number but that had -- those kind of things happen most quarter.

Rex A. Copeland - *Great Southern Bancorp, Inc. - Treasurer*

Not a material amount. I mean, if it was a large amount, wewould have put this information in the earnings release.

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

Yes.

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

Okay. And then just final question on the loan-to-deposit ratio. I mean, obviously, you guys are comfortable running above 100%. But with -- I think with the branch sale, what's that $55 million, $60 million in deposits. So you kind of go from [108]at the end of June to, all things equal, [109,]which sort of seems to be -- and I've covered you guys for a long time. That's sort of the upper end of the range over the past decade.

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

Yes. The thing is, we feel like we have a lot of runway with alternative, funding sources, broker CDs, those kinds of things. So we think there's no short-term need. And by that, I'm talking six quarters of relatively robust loan growth. I think beyond that, yes, our -- over the longer term, our deposits do need to grow along with our loans. And we've got plans -- I think our biggest advantage there is we do have a system of banking centers that are staffed, we're able to handle more deposits if we can bring them in. So that's number one. We do have the ability and sort of our, I guess, you would say a bit of a gangly franchise, we're able to go to metropolitan areas and offer specials at a little higher rate without repricing our entire portfolio. And then we're working pretty hard on an online product that we could offer nationwide. And I think we'll have something going on there by the end of the year, Kelly. So I think those would be our three longer-term strategies. In the short term though, we don't feel constrained. We don't feel unable to really aggressively pursue good loan opportunities because of a higher level of our -- higher loan-to-deposit ratio.

Rex A. Copeland - *Great Southern Bancorp, Inc. - Treasurer*

And you've covered us long enough, John, that you remember when we probably had -- 1/3 of our deposits were broker. So not that we would necessarily want to get to that level again. But we could certainly be much higher than the $100-and-some-million that we have at the end of the second quarter.

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

But as far as the loan-to-deposit ratio is there, I mean, I doubt it, does it go to [115 or 120.] Could it? Or...

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

Depending on how you calculate it, I guess. Yes, are you talking about loans, the core deposits?

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

No, just total deposits.

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

Well, I mean, we're going to be growing if our core deposits don't grow to fund loan opportunities. We'll probably be funding them with broker deposits. So yes, I mean, in that sense, that number probably wouldn't go much higher.

Operator

And I'm showing no further questions. I would now like to turn the call back to Ms. Kelly Polonus for any further remarks.

Kelly A. Polonus - *Great Southern Bancorp, Inc. - Director of Communications & Marketing for Great Southern Bank*

I believe that concludes our call. If anyone has any further questions, please feel free to contact me. If not, we will visit with you next quarter. Thanks for joining us.

Joseph William Turner - *Great Southern Bancorp, Inc. - President, CEO & Director*

Thanks everybody. Thank you.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program. You may all disconnect. Everyone, have a great day.